PROPOSALS CERTIFIED TO SAVE SOCIAL SECURITY

HEARING

BEFORE THE

COMMITTEE ON WAYS AND MEANS

HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

JUNE 9 AND 10, 1999

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COMMITTEE ON WAYS AND MEANS

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PROPOSALS CERTIFIED TO SAVE SOCIAL SECURITY

WEDNESDAY, JUNE 9, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, DC.

The Committee met, pursuant to notice, at 10:06 a.m., in room 1100, Longworth House Office Building, Hon. Bill Archer (Chairman of the Committee) presiding.

[The advisory announcing the hearing follows:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE
May 26, 1999
No. FC–9

CONTACT: (202) 225–1721

Archer Announces Hearing on Proposals Certified to Save Social Security

Congressman Bill Archer (R–TX), Chairman of the Committee on Ways and Means, today announced that the Committee will hold a 2-day hearing on proposals, offered by Members of Congress to strengthen Social Security, that would achieve 75-year solvency as estimated by the Social Security Administration's Office of the Chief Actuary. The first day of the hearing will take place on Wednesday, June 9, 1999, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 10:00 a.m. The hearing will be continued on Thursday, June 10, 1999, also in 1100 Longworth, beginning at 10:00 a.m.

Oral testimony will be heard from invited witnesses only. Invited witnesses will include Members of Congress who have introduced proposals that would restore Social Security's solvency over the next 75 years, as estimated by the Social Security Administration's Office of the Chief Actuary. Witnesses will also include a representative of the Social Security Administration's Office of the Chief Actuary. Any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

BACKGROUND:

According to the Social Security Board of Trustees 1999 Annual Report on the financial status of the Trust Funds, Social Security's annual spending is projected to exceed its annual income in the year 2014, and the Trust Funds will be depleted by the year 2034. In anticipation of Social Security's future funding shortfalls, several Members of the House and Senate have offered proposals that would strengthen Social Security's finances. Of particular note to the Committee are proposals that would restore the program's solvency for the upcoming 75-year period, the standard measure of the program's long-term solvency, as estimated by the Social Security Administration's Office of the Chief Actuary.

In announcing the hearing, Chairman Archer stated: "The Social Security proposals offered by Members of the House and Senate reveal many points of agreement regarding the best way to save Social Security. In order to resolve our differences and move ahead, we must build on these points of consensus. I am convinced that, if we work together, we will be able to save Social Security this year."

FOCUS OF THE HEARING:

The Committee will hear the views of those Members of the House and Senate who have introduced proposals to strengthen Social Security that would achieve 75-year solvency as estimated by the Social Security Administration's Office of the Chief Actuary. The Committee would like each witness to address: (1) the specific provisions of their plan, including a full explanation of any effects on taxes and benefits, (2) the effects of the plan on Social Security Trust Funds and cash flows, (3) the unified budget effects with financing costs, and (4) the use of general revenues.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Any person or organization wishing to submit a written statement for the printed record of the hearing should submit six (6) single-spaced copies of their statement, along with an IBM compatible 3.5-inch diskette in WordPerfect 5.1 format, with their name, address, and hearing date noted on a label, by the close of business, Thursday, June 24, 1999 , to A.L. Singleton, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, Room 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public at the hearing, they may deliver 200 additional copies for this purpose to the Committee office, Room 1102 Longworth House Office Building, by close of business the day before the hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be submitted on an IBM compatible 3.5-inch diskette in WordPerfect 5.1 format, typed in single space and may not exceed a total of 10 pages including attachments. Witnesses are advised that the Committee will rely on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. A witness appearing at a public hearing, or submitting a statement for the record of a public hearing, or submitting written comments in response to a published request for comments by the Committee, must include on his statement or submission a list of all clients, persons, or organizations on whose behalf the witness appears.

4. A supplemental sheet must accompany each statement listing the name, company, address, telephone and fax numbers where the witness or the designated representative may be reached. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press, and the public during the course of a public hearing may be submitted in other forms.

Note: All Committee advisories and news releases are available on the World Wide Web at “HTTP://WWW.HOUSE.GOV/WAYS_MEANS/”.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202–225–1721 or 202–226–3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman ARCHER. The Committee will come to order.

I know we were a little bit late in opening the doors and letting our visitors and guests and the public enter, but the Chair would encourage our visitors and guests to take seats as quickly as possible so we can commence the hearings. We are going to have a long day of hearings.

Good morning. As Social Security Subcommittee Chairman Clay Shaw likes to say, “If you say you are for saving Social Security,

now is the time to get out of the bleachers and onto the playingfield."

He is right. And that is precisely why we are here today. We need to move past posturing, partisanship, and politics and work together to get the job done. Indeed, the American people want Congress and the President to act now to save Social Security.

Speaker Hastert is committed to finding a bipartisan solution for Social Security, and without objection, I enter into the record a letter I received this morning from the Speaker. Among other things, the letter states the following, and I quote: "As Speaker, I truly believe that, through hard work and a strong commitment on both sides of the aisle and at both ends of Pennsylvania Avenue, consensus is possible. Today's hearing takes a step beyond the retirement security safe deposit box and another step closer to finding a credible proposal that saves and strengthens Social Security for 75 years and beyond."

This and other recent developments make me optimistic that we can save Social Security this year. I have personally met with President Clinton, and he has assured me that he is committed to finding a bipartisan solution. Likewise, my talks with our friends on the Minority side have offered hope. Everyone I believe does want to save Social Security. The question, of course, is: How and when?

There are several plans that would save Social Security for the requisite 75 years, and I congratulate every Senator and Member of the House with the courage and conviction to touch the so-called third rail of politics by introducing a plan. Now, our challenge is to assess each of these plans and find common ground among them, in hopes of building a bipartisan consensus to save Social Security. This cannot be done by one party. It is too important and touches the lives of every single American.

What is encouraging to me is that most of the plans we discuss today and tomorrow are a change from the past in that they offer new and innovative solutions to Social Security's problems. That is a welcomed change because history has shown that simply raising taxes and/or cutting benefits only delays the date of bankruptcy and will not save Social Security. I served on the 1982–83 commission and voted against the ultimate agreement for one primary reason: that it would not save Social Security for 75 years. And I made that point within the commission and in the debate on the floor of House. Unfortunately, I was right. And we are back today.

Today, we must save Social Security, predictably and objectively on a 75-year basis, and, yes, beyond for the next century. We owe it not only to current seniors and retirees, we owe it to those who have just been born—to my 13 grandchildren and to your grandchildren, whether they are here today or whether they will be coming sometime soon in the future.

Today's proposals offer a new direction. For example, almost all of the plans seek to increase Social Security's rate of return by taking advantage of the higher yields available in the private equity and bond markets. In addition, there is consensus that Social Security benefits should be at least partially funded in advance to take pressure off of future generations. There is not magic to how we solve the problem of the baby-boomer retirement, when we will

have only two workers for every retiree instead of three for every retiree today. It can be done only by two basic changes: presaving in advance; prefunding in advance and increases in productivity. Otherwise, our children and their children will be unable to bear the load of taking care of their elderly while, at the same time, improving their own standard of living. Unfortunately, we have not faced up to this in past years, but we are doing it today.

And finally, because we are projecting surpluses in the future, all of the plans before us rely on general revenues to varying degrees. So, there's common ground among the plans, and I encourage each of us here today to keep an open mind and a cooperative spirit as we discuss each plan in detail. If we continue to put principle before politics and ideas before ambition, we can save Social Security this year. As the President said, we have a once-in-a-blue-moon opportunity. The longer we wait, the tougher it will be.

Yes, Social Security will survive for 35 years under current projections. So why bother to work on it now? Why take on this difficult challenge? And the answer is very simple: if we do not, each Congress in succession will have a heavier load and a more difficult burden. We do need to prove that a democracy can plan in advance and not wait until it gets to the edge of a cliff.

Finally, I would announce that, for the first time since Chairman Rostenkowski did it in 1990, I will relinquish the gavel tomorrow and take the witness stand to testify on the Archer-Shaw Social Security Guarantee Plan. In my opinion, it is only fair to subject myself to the same joy and delight that all of the witnesses before us today will experience, and I am greatly looking forward to that opportunity.

[The following was subsequently received:]

J. Dennis Hastert
Fourteenth District
Illinois

(202) 225-0600

Office of the Speaker
United States House of Representatives
Washington, DC 20515

June 9, 1999

Chairman Bill Archer
House Ways & Means Committee
1102 Longworth
Washington, DC 20515

Dear Chairman ~~Archer~~: Bill

I want to applaud you and the members of your Committee for beginning to hold hearings on the future of Social Security. We must thoroughly examine the proposals before us that extend the life of this important retirement program for at least 75 years.

As you know, Congress already has begun taking steps to protect the Social Security surplus from being used for more government spending or tax relief. American workers should have the confidence that the money they pay into their retirement security system is only used for their retirement security. Just last month, the House passed legislation to lock away 100% of the retirement surplus in a safe deposit box so it could be used only for Social Security or Medicare.

Our challenge now is to find a bipartisan solution to save and strengthen Social Security for future generations. I would hope that today's hearing puts politics aside and begins a process that will lead to a bipartisan solution that preserves Social Security's long-term future.

I want to congratulate members on both sides of the aisle who have introduced or cosponsored plans to save Social Security for at least 75 years. As you begin this search for a bipartisan solution for Social Security, I would hope that both Republicans and Democrats will put Social Security first, and politics second -- progress, before partisanship.

As Speaker, I truly believe that through hard work and a strong commitment -- on both sides of the aisle and at both ends of Pennsylvania Avenue -- consensus is possible. Today's hearing takes a step beyond the retirement security safe deposit box and another step closer to finding a credible proposal that saves and strengthens Social Security for 75 years and beyond.

Sincerely,

J. Dennis Hastert
J. Dennis Hastert
Speaker of the House

Chairman ARCHER. And I now recognize Mr. Rangel for any statement that he might like to make in behalf of the Minority, and without objection, every Member will be able to enter into the record any written statement that they wish to make.

Mr. Rangel.

Mr. RANGEL. Thank you, Mr. Chairman. I ask unanimous consent that my full statement be placed in the record.

Chairman ARCHER. Without objection, so ordered.

Mr. RANGEL. And I volunteer to take the gavel while you testify. [Laughter.]

For whatever time, you know, you would be away.

Chairman ARCHER. Well, I know that the gentleman served during the Korean Conflict, and I am sure he is well prepared.

Mr. RANGEL. I want to thank you, Chairman Archer, for taking this courageous step forward in having the President and the Minority express their views on the sensitive, but important, issue of saving of Social Security, as well as for allowing us to have a better understanding as to exactly what the Shaw-Archer talking points are and would soon become. I look forward to your recommendations.

I do think that having these hearings and listening to Members that have their exciting plans is a good educational vehicle. I think the American people for the first time understand that, even though we do not have a program that is in immediate danger, the best time to deal with it is while we have a surplus. As other people have said, when the sun is shining is when you fix the roof.

All of the plans that we have to come up with have to have some fiscal pain because none of us want to raise taxes or to reduce benefits. I fail to understand why we have this obsession with 75-year solvency. Being 69 years old, I cannot really think that far ahead as to why this magic number was selected. I know we want to be responsible to our grandchildren, but there comes a time when we should be able to pick a year that is closer to our understanding.

If, in 1924, Congress had been looking 75 years into the future and had attempted to protect Social Security, with the same vigor, energy, and dedication as some people are today, Congress could not have predicted the Great Depression, World War II, Vietnam, the Persian Gulf, or Korea. So it just seems to me that, while we should do the best that we can, we should not get locked into just a 75-year goal. The only thing we would be doing then is committing ourselves to using general revenue to say that the fund would be there. I think that Social Security is already sensitive enough for future Congresses.

In any event, as we listen to all of these plans, I do hope, at some point, either at our hearings or at meetings that you would be inclined to call, that we can develop a process that could lead us toward bipartisanship, because I know that you agree that the only way that we can tackle this is in a bipartisan manner. It is not going to be done on C–SPAN, and it is not going to done with these mikes in front of us. We have to find out what areas of agreement and disagreement we have.

We have had the opportunity to pick apart the President's plan, which will be put into legislative form this week. I suspect that we will also be able to find some flaws in the Archer-Shaw plan, but while we are doing this, I do hope that the membership will keep a positive view in mind, because, after we have found the flaws, we have the responsibility to pick up the pieces and to move forward.

Now, I know that certain people believe that the second worst thing after being in the Minority is being in the Majority with six votes. Some people further believe that it would be to our benefit if we just ignored Social Security and asked the leadership to provide the votes on this and other key issues. I know that most Democrats do not feel this way. We truly believe that, if we can work together and show the American people that Social Security is above partisanship, it would help us in the elections as well as

help Republicans by getting people to come out and to understand that we can disagree, but that we all have the national interest at heart.

And so, Mr. Chairman, I do hope that as we have these public hearings and as Members share with us their views, there will be some vehicle where we can actually work together as Members of Congress, rather than Republicans and Democrats, to see what it is that we agree on, what are the differences and how we can work that out.

In any event, I want to thank you for calling these hearings and giving me this opportunity to speak on behalf of the Minority Democrats.

[The opening statements follow:]

Statement of Hon. Charles B. Rangel, a Representative in Congress from the State of New York

Today we will hear from a number of Members of Congress about the Social Security plans they have proposed. While I look forward to hearing the views of all Members present, I am particularly pleased to have the opportunity to examine the plan that the Chairman of this Committee and the Chairman of our Social Security Subcommittee announced over a month ago.

Since this is the first opportunity we have had to examine the Archer-Shaw plan as a Committee, I hope that we will be able to give the plan its full due today. Just as we subjected the President's plan to rigorous critical analysis earlier this year, we should direct our full attention to both the merits and shortcomings of the Archer-Shaw plan.

We should not allow ourselves to be distracted today by the politics surrounding Social Security reform. This is a time, not to make political points, but to make history. We can make history only by working together to craft a common solution, not by dividing ourselves into certain camps for political gain.

One possible area of common ground has been identified in the proposal offered today by Representative Pete Stark. There are many differences between the Archer Shaw proposal and the Stark plan to preserve Social Security. However, both direct a portion of the general revenue surplus (equivalent to 2% of the taxable payroll) into the Social Security system in order to achieve 75-year solvency. This similarity between Stark and Archer-Shaw may be just the starting point we need to start the process of negotiating bipartisan legislation that can become law this year.

That process needs to begin soon. While these hearings are better than nothing, action would be better than hearings. I applaud Chairman Archer for calling these hearings after his meeting with the President last month, but I would be surprised if new information came out of them. All of the proposals before us have been around for some time. My senior Senator (Moynihan) introduced a version of his plan in March of last year.

Soon, we will have to stop talking about all the various plans and start the negotiating process. Chairman Archer and Mr. Shaw have done much to push this process forward. They have shown much courage by putting forth their proposal even while their own Republican leadership preferred to avoid the issue. They have gone out of their way to meet with me and Mr. Matsui to discuss their plan and talk about places where we might find common ground.

Unfortunately, the hard work of this Committee will be in vain if the Republican leadership continues to sidestep the Social Security issue. We cannot come together in a bipartisan solution until each party's leadership is willing to put itself behind a plan. On the Democrats' side, the President has put forth a plan and we will introduce his plan as a bill in the coming weeks. On the Republican side, the Chairman and Mr. Shaw have their plan. However, the Republican leaders in both the House and Senate have distanced themselves from the Archer-Shaw proposal or any of the alternative proposals that will be discussed in these hearings.

The Republican leadership's priorities are apparent from the schedule for the next few months. According to the budget resolution the Republicans passed, this Committee is to report out, by July 16, a large tax bill that would consume a vast chunk of the budget surplus that we may need to save Social Security and Medicare. Democrats want to secure Social Security and Medicare first before we spend any of the surplus.

While we have a date set for tax breaks, we do not have a deadline for reporting Social Security reform out of this Committee nor do we have deadline for reporting Medicare reform. We do not have deadlines for action on these crucial issues because the Republican leadership would rather squander the budget surpluses on tax breaks, rather than reserving them until we have strengthened Social Security and Medicare.

When we have budget surpluses is our best chance to meet the challenges faced by the Social Security and Medicare systems. If we act now, we can strengthen Social Security and Medicare, extending their solvency while securing the same or better level of service. If we procrastinate too long, our job only gets tougher.

The time to fix the roof is when the sun is shining. Democrats and many Republicans in this room stand ready, tools in hand, to start work on fixing the roof. But the Republican leadership seems to prefer heading to the beach on sunny days and hoping the work mysteriously gets done anyway. Hopefully, Mr. Chairman, these hearings will serve not just to reiterate what has already been said, but also will sound a new call to action to strengthen and secure Social Security.

Statement of Hon. William J. Coyne, a Representative in Congress from the State of Pennsylvania

We are here today to discuss ways to strengthen one of our most important and successful government programs: Social Security. As we all know, the Social Security program, which has served millions of Americans over the last 60 years, will face a financial crisis in the coming decades. Because Social Security is so critical to American workers, our Committee has an obligation to save it first, before considering other priorities.

Social Security has made life better for millions of Americans. Before the Social Security program was established, half of Americans over the age of 65 lived in poverty. Today, only 10 percent of senior citizens live in poverty. In my Congressional district, half of all retirees get all of their income from Social Security.

Social Security also provides peace of mind for millions of workers, who are secure in the knowledge that Social Security will take care of them and their loved ones if they should die or become disabled. Over sixteen million people under 65 receive disability and survivor benefits from Social Security.

For our hearing today, Chairman Archer has set one important measure for all the plans we consider. A complete plan must extend Social Security's solvency to 75 years. However, I believe there are a number of other standards that must be met by a complete plan.

A complete plan will maintain Social Security's guaranteed benefit structure. It will not expose workers to the kind of risk Social Security was designed to prevent.

A complete plan will preserve Social Security's survivor and disability benefit for all workers and their families.

A complete plan will also provide for Medicare's future. Medicare is a critical part of the safety net for elderly people. Even with Medicare coverage, elderly people spend about a third of their income on health care.

I look forward to hearing the testimony today. I hope that our Committee will work together to report out a bipartisan plan which meets the standards I have outlined.

Statement of Hon. Jim Ramstad, a Representative in Congress from the State of Minnesota

Mr. Chairman, thank you for calling this important hearing to review the proposals that our colleagues have introduced to save Social Security.

As one who has always believed that we need to approach the issue of securing the long-term financial solvency of this vital program in a bipartisan, pragmatic way, I greatly appreciate the opportunity to thoroughly review each proposal that has been certified to keep Social Security solvent for another 75 years. Certainly, with a program this complex, yet this important, we need to review all options.

My constituents have told me at town meetings, and through calls and letters, that they want real improvements to be made so Social Security is operating as promised for current and future beneficiaries. They also do not want taxes raised or benefits cut. Most importantly, they believe financial soundness is paramount in

the design of any new system. These are some of the basic elements I will be looking for in each proposal reviewed today.

I also want to take a moment to thank the authors of all of these proposals for having the courage to introduce them. Knowing how sensitive the topic of Social Security is, I can only imagine how long it took for the Members to study all of the details, consult with experts, interest groups and constituents in designing their plans.

While we may not agree on which approaches are best, I know we are all committed to saving this important program. I look forward to learning more today from our witnesses about the elements of their proposals.

Chairman ARCHER. I thank the gentleman.

Before recognizing our first witness, I should alert the Committee and the witnesses that, whereas our standard rule is a 5-minute presentation by a witness, inasmuch as these plans are, to some degree, complex and certainly comprehensive, the Chair will permit a 10-minute presentation by each of the witnesses verbally, and, of course, their written statement, without objection, will be included in the record. But the Chair intends to strictly enforce that 10-minute rule, and I am reluctant to say that in the presence of some of our Senate colleagues, who are used to speaking without limitation, but I hope that they will be able to comply with that extension of the House rule.

And without objection, I would like to place into the record at this point copies of all the letters from the Social Security actuaries on the various plans that we are considering today in this hearing.

[The information follows:]

SOCIAL SECURITY ADMINISTRATION
April 29, 1999

Harry C. Ballantyne
Chief Actuary

MEMORANDUM

Refer To: TCC

Subject: Long-Range OASDI Financial Effects of the Social Security Guarantee Plan—INFORMATION

This memorandum provides long-range estimates of the financial effects on the Social Security (OASDI) program for enactment of the Social Security Guarantee (SSG) Plan proposed by Representatives Archer and Shaw. This plan would provide for an annual contribution from the General Fund of the Treasury to SSG individual accounts equal to 2 percent of each worker's OASDI taxable earnings beginning with earnings in 1999.

Proceeds from these accounts would, commencing at the worker's retirement (or disability), be transferred entirely to the OASDI trust funds on a gradual basis. For workers who die before OASDI benefit entitlement without potentially eligible survivors, the account balance would go to the worker's estate, tax free. Benefits paid by the OASDI program would be the higher of benefits scheduled under current law or the scheduled SSG withdrawal rate based on a life-annuity calculation.

The combined OASDI payroll tax of 12.4 percent (6.2 percent for employees and employers, each) is assumed to be reduced in future years under the intermediate assumptions of the 1999 Trustees Report and expected investment yields. The proposal would also include the gradual elimination of the Social Security retirement earnings test between 2001 and 2006.

Enactment of this proposal, as specified, would be expected to eliminate the estimated long-range OASDI actuarial deficit (2.07 percent of taxable payroll under present law). Under assumptions described below, revenue transferred from the SSG accounts to the trust funds would be sufficient to allow reductions in the combined OASDI payroll tax rate of 2.5 percentage points in 2050 (from 12.4 to 9.9 percent) and 1 percentage point in 2060 (to 8.9 percent).

Estimates are provided for the SSG plan with and without the specified payroll tax reductions. Estimates are also provided to illustrate the sensitivity of the plan to possible variation in the yield on SSG accounts.

All estimates assume elimination of the OASDI retirement earnings test for ages 62 and older, gradually between 2001 and 2006. (This change has a very small effect on the long-range financial status of the OASDI program.) All estimates in this memorandum are based on the intermediate assumptions of the 1999 Trustees Report, except as indicated below.

The Proposal

Contributions and Investment Up To Benefit Entitlement

The proposal would provide Social Security covered workers with refundable tax credits equivalent to 2 percent of their OASDI taxable earnings for calendar years starting 1999. Credits would be increased with interest from July 1 of the year of taxable earnings, at the market yield on publicly-held Federal debt, until paid. Credits would be paid from the General Fund of the Treasury on October 15 (December 1 for self-employment earnings) in the following calendar year for the sole purpose of deposit in a SSG account. Credits for earnings in 1999 would be delayed one additional year and paid in 2001.

Accounts would be managed by mutual funds, qualified and supervised by the Social Security Guarantee (SSG) Board. The Board would consist of the six individuals appointed by the Social Security (OASDI) Trustees.

Individuals would be required to hold all SSG assets in a single fund and could change funds at most once per year. Annual SSG credits would be pooled and transmitted to the mutual fund managers by a central agency. Account holders would receive annual notice of assets in their Social Security Personal Earnings and Benefit Statements.

The proposal requires that all account balances be invested in qualified mutual funds maintained with a portfolio allocation of 60 percent stock index funds and 40 percent corporate bonds. The charge for annual administrative expenses would be limited to 25 basis points (excess expense, if any would be made up from the General Fund of the Treasury). Withdrawals prior to reaching retirement (or disability) would not be permitted.

Earnings Test Elimination at Age 62+

The Social Security retirement earnings test annual exempt amounts would be raised according to a specified schedule through 2005, and the test would be eliminated starting 2006, for all beneficiaries age 62 or older. For beneficiaries under age 62, the current test would remain unchanged. The exempt amounts would be specified for the test applicable at ages NRA through 69 as $35,000 for 2003, $40,000 for 2004, and $45,000 for 2005. For the test applicable at ages 62 up to NRA, the exempt amounts for years 2001 through 2005 would be set at $15,000, $20,000, $25,000, $30,000, and $35,000, respectively. This provision alone would have a negligible effect (between 0.005 and −0.005 percent of taxable payroll) on the OASDI actuarial balance.

SSG Account Distributions

Under the plan, the SSG account balance of workers who become entitled to OASDI retirement or disability benefits would ultimately be transferred entirely to the OASDI trust funds. Upon entitlement for Social Security retirement or disability benefits, the Social Security Administration would compute the monthly payment that could be provided from a life annuity purchased with the holdings in the SSG account. The annuity calculation would reflect the anticipated yield on the SSG account (60 percent stock and 40 percent corporate bonds, less 25 basis points for administration) and indexing of annuity payments for price inflation (as for the Social Security COLA). The annuity calculation would also reflect the expected payment of aged spouse and aged survivor benefits if the worker has a current spouse and/or a qualifying divorced spouse (marriage lasted 10 years or longer).

If the computed monthly annuity amount exceeds the level of current law scheduled OASDI benefits, then the Social Security Administration would guarantee payment from the trust funds of the computed annuity amount for life. If the computed annuity amount is less than the level of the OASDI benefit, then the OASDI benefit would be payable for life. Each month after benefit entitlement the computed annuity amount based on entitlement of the worker and any aged spouse(s) would be transferred from the SSG account to the OASDI trust funds.

Because the computed annuity amount is based on a life annuity calculation, the SSG account would be expected to be depleted at the point where the bene-

ficiary(ies) reach their life expectancy, as estimated at the time of benefit entitlement. Thus, for about half of the SSG accounts, benefits will be payable after exhaustion of the SSG account entirely at the expense of the OASDI trust funds. For the other half, death before life expectancy will leave remaining SSG balances for the payment of benefits to those who lived beyond life expectancy. For workers who die prior to exhausting their SSG account, but after becoming entitled to OASDI retirement or disability benefits, the remaining balance in the SSG account will be transferred to the account of any surviving spouse potentially eligible for benefits payable by OASDI (as a surviving spouse or surviving divorced spouse). At the point at which a worker has died, and each spouse or qualifying divorced spouse has also died, any remaining SSG account balance will be transferred to the OASDI trust funds.

For workers who die before becoming entitled to OASDI retirement or disability benefits, the balance in the SSG account will be transferred to the account of any surviving spouse potentially eligible for benefits payable by OASDI (as a surviving spouse or surviving divorced spouse). If children of the worker who are eligible for survivor benefits survive the worker and any spouse, the SSG account will be maintained to cover these benefits. At the point at which a worker has died (prior to entitlement to any OASDI benefit), and each spouse or qualifying divorced spouse has also died (prior to entitlement to any OASDI benefit), and there are no eligible children, any remaining SSG account balance will go to the estate of the deceased, tax free.

OASDI Payroll Tax Rate Reduction

The plan calls for a reduction in the OASDI combined payroll tax rate from 12.4 percent to 9.9 percent in 2050 and to 8.9 percent in 2060. These reductions reflect the specified SSG portfolio allocation with the assumed asset yields described below. Payroll tax rate reductions are assumed to be implemented if transfers from the SSG accounts to the trust funds are large enough to raise the OASDI trust fund ratio above 200 percent, with continued increase thereafter.

ASSUMPTIONS

SSG Account Accumulation

SSG account portfolios are required to be invested, both prior to retirement (or disability) benefit entitlement and after benefit entitlement in qualified SSG funds that are must be maintained at 60 percent stock and 40 percent corporate bonds, with an annual administrative expense charge of 25 basis points. The long-term ultimate average real yield on stocks is assumed to be 7 percent, as assumed by the 1994–96 Advisory Council. (It should be noted that while the real yield on stocks has averaged 7 percent so far this century, many speculate that future yield may average less.) The ultimate real yield on long-term corporate bonds is assumed to average 3.5 percent, or 0.5 percentage point higher than the 3.0 percent real yield for U.S. Government long-term securities, as assumed for the 1999 Trustees Report. This spread between corporate and U.S. Government bond yields is consistent with the spread experienced over the past 40 or 70 years, on average. It should be noted, however, the spread has been much smaller over the past 20 years. The expected ultimate real portfolio yield for the base projection (alternative 1) would thus be 5.35 percent, net of administrative expense,

$$(0.6 * 7\% + 0.4 * 3.5\% - 0.25\% = 5.35).$$

A range of administrative expense factors was assumed for individual accounts proposed by the 1994–96 Advisory Council on Social Security. For the Individual Account (IA) plan, individual contributions were assumed to be collected and recorded by central institution, invested in large blocks with financial institutions, and invested in a limited number of indexed funds. Based on experience of TIAA and the Federal Employee Thrift Savings Plan (TSP) it was assumed that the IA plan could be administered with an expense of 10.5 basis points per year. For the Personal Security Accounts (PSAs), individual accounts were assumed to be invested on an individual basis, resulting in an annual administrative expense of 100 basis points. Because the description of SSG individual accounts is far closer to the individual accounts for the IA plan than to the individual accounts for the PSA plan, the specified administrative expense factor of 25 basis points for SSG accounts appears to be reasonable.

Distribution of SSG Accounts

Life annuity calculations for the purpose of determining the size of monthly transfers from SSG balances to the OASDI trust funds assume a real yield equal to the net expected real yield on SSG accounts, as specified. Mortality estimates for these calculations are based on the intermediate projections of the 1999 trustees report.

Annuity calculations are assumed to be made on a unisex basis for workers with no spouse or qualified divorced spouse (marriage lasting at least 10 years). For those with a spouse, annuity calculations would be on a joint and survivor basis intended to roughly match the expected payment of OASDI benefits. For the purpose of these calculations, a joint and 2/3 survivor annuity is assumed. Thus, the amounts transferred to OASDI from the SSG account of a married beneficiary would be reduced by 1/3 upon the death of either the worker or the spouse.

Under the SSG account yields assumed for these estimates, expected transfers from SSG accounts after benefit entitlement would be less than expected OASDI benefits for virtually all future beneficiaries. However, single workers with very high earnings, close to or above the OASDI maximum taxable amount throughout their careers would have transfers from their SSG accounts greater than current law benefits if the investment return during their working years exceeded the assumed long-range average return used for these estimates. High-earning married workers would be far less likely to have transfers that exceed current-law benefits because the joint-and-survivor annuity calculation would provide lower transfers than for single workers, and current law OASDI benefits for married workers would tend to be higher.

Estimated Effect On OASDI Financing

The table below provides the estimated OASDI actuarial balance, the change in the actuarial balance, and the estimated year of combined OASDI trust fund exhaustion for the SSG Plan as described above. To illustrate the full extent of the expected value of transfers from the SSG accounts to the OASDI trust funds, the estimated financial effects of the SSG Plan without the specified reductions in the OASDI payroll tax rate are also included in the table below.

Under the SSG Plan, the OASDI actuarial balance would be improved by 2.15 percent of effective taxable payroll, from a balance of −2.07 percent under current law to a positive balance of 0.09 percent of payroll under the plan. The OASDI trust fund as a percent of annual OASDI outgo (the trust fund ratio) would be expected to remain positive throughout the long-range 75-year projection period, thus allowing timely payment of benefits in full through 2073, and beyond. The trust fund ratio would be expected to decline to about 132 percent at the beginning of 2041, and to increase thereafter. The combined OASDI payroll tax rate would be reduced from 12.4 percent to 9.9 percent for the period 2050 through 2059 and to 8.9 percent for 2060 and later. Even with these reductions in the payroll tax rate, the trust fund ratio would be expected to be stable at about 240 percent of annual outgo at the end of the long-range 75-year projection period. See table 1a attached for details.

Estimated Effects on OASDI Financial Status of the Social Security Guarantee (SSG) Plan

(percent of taxable payroll)

	Estimated OASDI Actuarial Balance	Estimated Change in OASDI Actuarial Balance	Year Exhaust OASDI Trust Funds
Present Law (No SSG)	−2.07	—	2034
SSG Plan [1]			
60% Stock, 40% Corp Bond			
Assess only .25% Admin Cost	+0.09	2.15	NA
Illustration of SSG Plan Without Reduced Payroll Tax			
60% Stock, 40% Corp Bond			
Assess only .25% Admin Cost	+0.65	2.71	NA

[1] Payroll tax rate would be reduced from 12.4 to 9.9 in 2050 and 8.9 in 2060.

Based on intermediate assumptions of the 1999 Trustees Report and other assumptions described in the text.

The table above also includes an illustration of the potential financial effect of the SSG Plan on Social Security if the specified reductions in the OASDI payroll tax rate were not included. This provides an indication of the full effect on OASDI of the expected transfers from SSG accounts to OASDI trust funds under the plan.

Without the specified payroll tax rate reduction, the OASDI actuarial balance would be improved by 2.71 percent of taxable payroll, from a balance of −2.07 percent under current law to a positive balance of 0.65 percent of payroll under the plan without specified payroll tax rate reduction. Without the payroll tax rate reduction, the OASDI trust fund ratio would be expected to rise to over 10 times annual outgo by the end of the long-range period due to the magnitude of transfers from the SSG accounts.

Sensitivity to SSG Account Investment Yields

The effect of the SSG Plan on the financial status of the OASDI program depends greatly on the actual yield that is achieved for investments in the SSG accounts. Returns on all investments are uncertain, and returns on stocks are particularly variable over time. For this reason it is important to consider the sensitivity of the financial status of the OASDI program to possible variation in expected investment yield. Note that the 1999 Trustees Report provides this sensitivity analysis for the OASDI program under current law on page 138.

The table below provides the estimated OASDI actuarial balance, the change in the actuarial balance, and the estimated year of combined OASDI trust fund exhaustion for the SSG Plan with two different SSG yield assumptions in order to illustrate the sensitivity of the proposal to possible variation in the ultimate average returns on stock and corporate bonds.

Under sensitivity illustration 2, the average yield on SSG accounts is assumed to be 1 percentage point higher than expected for the accounts invested in 60 percent stock and 40 percent corporate bonds. Under this illustration, the OASDI trust fund ratio would be expected to decline to about 215 percent at the beginning of 2036, and to increase thereafter. The actuarial deficit would be eliminated under the SSG plan, and the combined OASDI payroll tax rate could be reduced from 12.4 percent to 9.4 percent for 2040 to2049, 6.4 percent for 2050 to 2059, and 4.4 percent for 2060 and later. Even with these reductions in the payroll tax rate, the trust fund ratio would be expected to be stable at about 300 percent at the end of the long-range 75-year projection period and the actuarial balance would be estimate positive 0.07 percent of payroll. Without the reduced payroll tax rate, illustration 2A, the OASDI trust fund ratio would be expected to rise to more than 50 times annual OASDI net cost (net of SSG transfers) by the end of the long-range period and the actuarial balance would be a positive 1.69 percent of payroll.

Sensitivity Analysis: Effect of Variation in Expected SSG Investment Yield Rates on OASDI Financial Status

(percent of taxable payroll)

	Estimated OASDI Actuarial Balance	Estimated Change in OASDI Actuarial Balance	Year Exhaust OASDI Trust Funds
Present Law (No SSG)	−2.07	—	2034
2: SSG Plan with 1% Higher Than Expected Yield[2] 6.35% average net yield	+0.07	2.13	NA
2A: SSG Plan with 1% Higher Than Expected Yield Without Reduced Payroll Tax 6.35% average net yield	+1.69	3.76	NA
3A: SSG Plan with 1% Lower Than Expected Yield[3] 4.35% average net yield	−0.08	1.98	2048

[1] Payroll tax rate reduced to 9.4 in 2040, 6.4 in 2050, and 4.4 in 2060.
[2] No payroll tax rate reduction.
Based on intermediate assumptions of the 1999 Trustees Report and other assumptions described in the text.

Under sensitivity illustration 3A, the average yield on SSG accounts is assumed to be 1 percentage point lower than expected for the accounts invested in 60 percent stock and 40 percent corporate bonds. Under this illustration, the OASDI trust fund ratio would be expected to become exhausted in 2048. However, the OASDI actuarial balance would be improved by about 1.98 percent of taxable payroll under this assumption, leaving an actuarial deficit of only 0.08 percent of payroll.

Annual Estimates of SSG Fund Operations and Estimated Effects on the Unified Budget Balance

Tables 1b, attached, provides estimates of aggregate SSG account balances, total contributions to and transfers from SSG accounts, and rough estimates of the effects

of other changes to the OASDI program (earnings test elimination). A very rough estimate of the effects of the SSG Plan on the annual Federal unified budget balance for calendar years 2000 and later is also provided.

These estimates are based completely on the intermediate assumptions of the 1999 Trustees Report, including the trust-fund interest assumption, and thus are not consistent with projections made by CBO and OMB (which use different assumptions. However, differences in payroll and benefit estimates are not large during the first 10 projection years so these values can be viewed as very rough approximations of the magnitude of effects on the unified budget balances through this period.

Under the SSG plan with the expected yield on the specified account portfolio, amounts transferred from the SSG accounts to the OASDI trust funds would at first be small, but would exceed credits to the SSG accounts from the General Fund of the Treasury by about 2031. Including the relatively small effects of the elimination of the earnings test at ages 62 and above, the estimated change in the unified budget "cash flow" (excluding interest effects) would also be negative until 2031. Including the cumulative effects of interest and the change in the OASDI payroll tax rate, the year in which the effect of the SSG plan on the unified budget annual balance would be expected to become permanently positive is 2054.

STEPHEN C. GOSS
Deputy Chief Actuary

Attachments

Table 1 a 2% SSG Account, Self Ann, 100% Benefit Offset, Elim Earns Test IA Cntrb 2 %. Ben Offset 100.0 %

SSG to Heirs With Ult Real TF Int Rate of 3.0

at Death < 65 With Ult Real IA Yld Rate of 5.35

If No Survivor With Annuity Net Yld Rate 5.35

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.79	12.65	1.86	217		12.40	0.00
2001	10.86	12.68	1.81	237		12.40	4.00
2002	10.97	12.68	1.71	256		12.40	2.00
2003	11.06	12.68	1.63	273		12.40	2.00
2004	11.16	12.69	1.53	289		12.40	2.00
2005	11.25	12.70	1.45	303		12.40	2.00
2006	11.36	12.71	1.35	315		12.40	2.00
2007	11.45	12.72	1.27	327		12.40	2.00
2008	11.56	12.73	1.17	338		12.40	2.00
2009	11.70	12.74	1.04	347		12.40	2.00
2010	11.85	12.75	0.90	354		12.40	2.00
2011	12.02	12.76	0.74	361		12.40	2.00
2012	12.23	12.77	0.54	366		12.40	2.00
2013	12.46	12.79	0.33	369		12.40	2.00
2014	12.71	12.80	0.10	370		12.40	2.00
2015	12.97	12.82	-0.15	370		12.40	2.00
2016	13.24	12.84	-0.40	367		12.40	2.00
2017	13.52	12.86	-0.67	363		12.40	2.00
2018	13.80	12.87	-0.93	357		12.40	2.00
2019	14.09	12.89	-1.20	350		12.40	2.00
2020	14.38	12.91	-1.46	341		12.40	2.00
2021	14.64	12.94	-1.70	331		12.40	2.00
2022	14.86	12.95	-1.90	321		12.40	2.00
2023	15.07	12.97	-2.09	311		12.40	2.00
2024	15.25	12.99	-2.26	299		12.40	2.00
2025	15.41	13.01	-2.40	287		12.40	2.00
2026	15.55	13.03	-2.52	275		12.40	2.00
2027	15.66	13.04	-2.61	262		12.40	2.00
2028	15.73	13.06	-2.67	250		12.40	2.00
2029	15.77	13.07	-2.69	237		12.40	2.00
2030	15.77	13.09	-2.68	225		12.40	2.00
2031	15.74	13.10	-2.64	212		12.40	2.00
2032	15.70	13.11	-2.58	200		12.40	2.00
2033	15.62	13.13	-2.49	188		12.40	2.00
2034	15.49	13.13	-2.36	178		12.40	2.00
2035	15.33	13.14	-2.19	167		12.40	2.00
2036	15.14	13.15	-1.99	158		12.40	2.00
2037	14.93	13.15	-1.78	150		12.40	2.00
2038	14.69	13.16	-1.54	143		12.40	2.00
2039	14.44	13.16	-1.28	138		12.40	2.00
2040	14.18	13.17	-1.01	134		12.40	2.00
2041	13.90	13.17	-0.73	132		12.40	2.00
2042	13.64	13.18	-0.47	132		12.40	2.00
2043	13.39	13.18	-0.21	134		12.40	2.00
2044	13.15	13.18	0.04	137		12.40	2.00
2045	12.91	13.19	0.28	143		12.40	2.00
2046	12.67	13.19	0.52	150		12.40	2.00
2047	12.45	13.20	0.75	160		12.40	2.00
2048	12.24	13.20	0.97	172		12.40	2.00
2049	12.03	13.21	1.17	186		12.40	2.00
2050	11.84	10.71	-1.13	203	-2.50	9.90	2.00
2051	11.67	10.72	-0.95	201		9.90	2.00
2052	11.51	10.72	-0.79	199		9.90	2.00
2053	11.37	10.73	-0.64	199		9.90	2.00
2054	11.24	10.74	-0.50	200		9.90	2.00
2055	11.11	10.75	-0.37	201		9.90	2.00
2056	11.00	10.75	-0.25	204		9.90	2.00
2057	10.89	10.76	-0.13	208		9.90	2.00
2058	10.79	10.77	-0.02	213		9.90	2.00
2059	10.70	10.78	0.08	219		9.90	2.00
2060	10.61	9.78	-0.83	226	-1.00	8.90	2.00
2061	10.53	9.79	-0.74	224		8.90	2.00
2062	10.45	9.79	-0.65	224		8.90	2.00
2063	10.38	9.80	-0.58	223		8.90	2.00
2064	10.31	9.81	-0.51	224		8.90	2.00
2065	10.26	9.81	-0.45	224		8.90	2.00
2066	10.21	9.82	-0.39	226		8.90	2.00
2067	10.17	9.82	-0.35	227		8.90	2.00
2068	10.14	9.83	-0.31	229		8.90	2.00
2069	10.11	9.83	-0.28	231		8.90	2.00
2070	10.10	9.83	-0.26	233		8.90	2.00
2071	10.09	9.84	-0.25	236		8.90	2.00
2072	10.09	9.84	-0.25	238		8.90	2.00
2073	10.10	9.85	-0.25	240		8.90	2.00
2074	10.11	9.85	-0.26	242		8.90	2.00
	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal			
1999 -2073	12.84	12.92	0.09	2.15			

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset

Office of the Actuary
Social Security Administration
April 28, 1999

Table 1 b IA Contributions, Transfers to OASDI from IA, & Unified Budget Effect

99 TR ECON — IA Cntrb 2 %, Benefit Offset 100.0 %

Year	IA Account Balance at End of Year	Amount Contrb to IA % by GenFnc 100	Transfer to OASDI from IA	Other Changes in OASDI CashFlow	Change in Annual UnifBudg CashFlow	Change in Debt Held by Public (EOY)	Change in Ann UnifBudg Balance
	(Billions of Current $)						
2000	0.0	0.0	0.0	0.0	0.0	0.0	0.0
2001	159.6	157.9	0.0	-1.5	-159.3	-164.1	-164.1
2002	256.1	82.2	0.2	-2.5	-84.5	-261.0	-96.8
2003	363.8	85.7	0.5	-3.4	-88.6	-367.7	-106.7
2004	483.6	89.6	1.0	-4.3	-92.9	-484.9	-117.2
2005	617.0	93.9	1.5	-5.0	-97.3	-613.5	-128.6
2006	765.2	98.4	2.5	-5.8	-101.8	-754.5	-141.0
2007	929.7	103.2	3.5	-5.7	-105.4	-907.9	-153.3
2008	1,112.0	108.3	4.9	-5.4	-108.8	-1,074.3	-166.5
2009	1,314.0	113.7	6.5	-5.2	-112.3	-1,255.3	-181.0
2010	1,537.7	119.3	8.6	-4.9	-115.6	-1,451.7	-196.4
2011	1,785.0	125.1	11.0	-4.8	-118.7	-1,664.6	-212.9
2012	2,057.9	131.0	14.0	-4.4	-121.5	-1,895.0	-230.4
2013	2,358.7	137.2	17.5	-4.3	-124.0	-2,144.2	-249.2
2014	2,689.0	143.6	21.6	-4.2	-126.1	-2,411.0	-267.3
2015	3,049.9	150.2	26.4	-4.0	-127.8	-2,697.7	-286.1
2016	3,443.5	157.0	32.0	-3.8	-128.8	-3,003.2	-305.5
2017	3,872.0	164.1	38.5	-3.7	-129.3	-3,328.7	-325.5
2018	4,337.7	171.5	46.1	-3.6	-129.1	-3,674.8	-346.1
2019	4,842.9	179.2	54.7	-3.5	-128.0	-4,042.0	-367.2
2020	5,390.1	187.1	64.6	-3.5	-126.0	-4,430.6	-388.6
2021	5,981.7	195.3	75.9	-3.4	-122.8	-4,840.8	-410.2
2022	6,620.3	204.0	88.8	-2.4	-117.6	-5,271.9	-431.0
2023	7,308.8	212.8	103.3	-1.2	-110.7	-5,723.4	-451.5
2024	8,049.1	222.1	119.8	0.1	-102.2	-6,195.0	-471.6
2025	8,844.7	231.8	138.4	1.5	-91.8	-6,686.2	-491.1
2026	9,698.0	241.9	159.3	3.1	-79.4	-7,195.9	-509.8
2027	10,611.9	252.4	182.8	4.2	-65.4	-7,723.8	-527.9
2028	11,569.2	263.4	209.1	5.4	-49.0	-8,268.6	-544.8
2029	12,632.7	275.1	238.4	6.6	-30.1	-8,828.8	-560.1
2030	13,745.1	287.3	271.2	7.9	-8.2	-9,402.2	-573.5
2031	14,929.2	300.0	307.6	9.2	16.8	-9,986.6	-584.3
2032	16,187.4	313.4	348.1	10.1	44.8	-10,579.4	-592.8
2033	17,522.0	327.3	393.0	11.0	76.7	-11,177.2	-597.9
2034	18,935.2	341.9	442.7	11.9	112.7	-11,776.2	-599.0
2035	20,429.0	357.2	497.6	12.8	153.3	-12,371.7	-595.5
2036	22,004.9	373.2	558.3	13.8	198.9	-12,958.3	-586.5
2037	23,664.1	390.0	625.3	14.9	250.1	-13,529.6	-571.2
2038	25,407.3	407.5	699.1	15.8	307.5	-14,078.1	-548.6
2039	27,234.4	425.7	780.4	16.9	371.6	-14,595.6	-517.5
2040	29,144.8	444.6	869.8	18.0	443.2	-15,072.4	-476.8
2041	31,136.9	464.3	968.1	19.2	523.0	-15,497.4	-425.0
2042	33,213.8	484.8	1,070.9	19.9	605.9	-15,864.1	-366.6
2043	35,376.4	506.2	1,180.6	20.6	695.0	-16,162.3	-298.2
2044	37,625.0	528.4	1,297.6	21.4	790.6	-16,381.0	-218.7
2045	39,960.0	551.5	1,422.2	22.2	892.9	-16,508.2	-127.2
2046	42,381.5	575.7	1,554.6	23.0	1,002.0	-16,531.0	-22.8
2047	44,889.2	600.7	1,695.1	23.9	1,118.3	-16,435.3	95.7
2048	47,482.8	626.8	1,843.9	24.8	1,241.9	-16,206.1	229.3
2049	50,161.5	654.0	2,001.3	25.7	1,373.0	-15,826.8	379.2
2050	52,924.5	682.2	2,167.4	-826.1	659.1	-16,159.8	-332.9
2051	55,770.5	711.6	2,342.5	-861.8	769.0	-16,400.6	-240.8
2052	58,698.3	742.2	2,526.6	-898.9	885.5	-16,536.6	-136.0
2053	61,706.1	774.0	2,720.1	-937.6	1,008.5	-16,554.6	-17.9
2054	64,792.3	807.3	2,922.9	-977.9	1,137.7	-16,440.3	114.3
2055	67,964.7	841.9	3,135.3	-1,019.9	1,273.5	-18,178.6	261.6
2056	71,191.1	878.0	3,357.3	-1,063.6	1,415.6	-15,753.7	424.9
2057	74,499.2	915.7	3,588.9	-1,109.3	1,563.9	-15,148.7	605.0
2058	77,876.4	955.0	3,830.1	-1,157.0	1,718.1	-14,345.8	802.9
2059	81,320.0	998.1	4,081.1	-1,206.8	1,878.2	-13,326.4	1,019.4
2060	84,827.3	1,038.9	4,341.7	-1,778.3	1,624.5	-12,606.6	719.8
2061	88,395.1	1,083.8	4,611.9	-1,854.9	1,673.4	-11,687.2	919.4
2062	92,020.4	1,130.3	4,891.8	-1,934.4	1,827.1	-10,550.4	1,136.8
2063	95,699.9	1,179.0	5,181.1	-2,017.2	1,984.9	-9,178.1	1,372.3
2064	99,430.4	1,229.9	5,480.0	-2,103.9	2,146.2	-7,551.6	1,626.5
2065	103,208.0	1,282.9	5,788.4	-2,194.0	2,311.5	-5,650.5	1,901.1
2066	107,028.8	1,338.1	6,106.3	-2,288.0	2,480.2	-3,453.8	2,196.8
2067	110,888.5	1,395.7	6,434.0	-2,386.0	2,652.2	-939.0	2,514.8
2068	114,782.3	1,455.8	6,771.4	-2,488.2	2,827.4	1,917.4	2,856.4
2069	118,704.9	1,518.4	7,118.9	-2,594.7	3,005.8	5,140.5	3,223.2
2070	122,660.2	1,583.6	7,476.6	-2,706.6	3,187.4	8,757.3	3,616.7
2071	126,611.4	1,651.6	7,845.2	-2,821.1	3,372.5	12,798.3	4,039.1
2072	130,580.5	1,722.4	8,225.0	-2,941.4	3,561.2	17,288.5	4,492.2
2073	134,648.3	1,796.2	8,616.7	-3,066.7	3,753.8	22,266.8	4,978.3
2074	138,493.3	1,877.2	9,034.8	-3,204.4	3,953.2	27,769.4	5,502.6

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.0 TF,

Ultimate Real Yield Rate of IA 5.35
Annuity Yield 5.35

Office of the Actuary
Social Security Administration
April 28, 1999

SOCIAL SECURITY ADMINISTRATION
June 6, 1999

Harry Ballantyne
Chief Actuary

MEMORANDUM

Refer To: TCC

Subject: Estimated Long-Range OASDI Financial Effect of the Draft Social Security Financial Solvency Act of 1999—INFORMATION

This memorandum provides the estimated effect on long-range OASDI financial status of the draft Social Security Financial Solvency Act of 1999. This proposal was provided in draft by Sandy Wise and Al Davis, minority staff for the House Ways and Means Subcommittee on Social Security. Estimates are based on the intermediate assumptions of the 1999 Trustees Report.

The proposal would provide for transfers from the General Fund of the Treasury, for each year starting 1999. Transfers each year would be in an amount equal to 2.07 percent of taxable Social Security payroll (TSSP). TSSP is defined as the sum of wages and self-employment income, as defined in the Social Security Act. TSSP, or taxable earnings, is thus equal to the total amount of earned income subject to any of the payroll tax on wages and self-employment income.

The TSSP amount is slightly higher than the OASDI effective taxable payroll (ETP). These values differ in two ways. First, ETP includes deemed military wage credits, which are excluded from taxable earnings (TSSP). Second, ETP includes only one half of wage earnings that are subject to employer tax only (these are referred to as multi-employer excess earnings). For an employee with more than one employer during a year, the employee's total taxable earnings from all employers for the year is limited to the taxable maximum. Each employer's taxable amount reflects only the wages that that employer paid to the employee.

This proposal would increase the income rate for the OASDI program by 2.076 percent of effective taxable payroll, improving the OASDI actuarial balance by the same amount. The long-range OASDI actuarial deficit of 2.07 percent of effective taxable payroll, under present law, would thus become a positive actuarial balance of 0.01 percent of effective taxable payroll under this proposal.

The projected OASDI combined trust fund assets, as a percent of annual cost, would be expected to rise to a peak of 648 percent in 2018, and would decline thereafter reaching an expected level of 108 percent at the end of the 75-year long-range period. At the end of the period, the combined trust fund would be declining as a percent of annual cost by about 20 percentage points per year. The attached table provides year-by-year projections of the expected long-range financial status of the OASDI program.

STEPHEN C. GOSS
Deputy Chief Actuary

Attachment

Stark 6/6 Memo

Table 1 a Social Security Fin Solv Act of 1999--Transfer 2.07% taxab erns IA Cntrb 0 %, Ben Offset 0.0 %

With Ult Real TF Int Rate of 3.0

With Ult Real IA Yld Rate of

With Annuity Net Yld Rate

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	14.78	3.98	194	2.076	14.48	0
2000	10.79	14.73	3.94	236	0.000	14.48	-0.00
2001	10.83	14.75	3.92	277	0.000	14.48	0.00
2002	10.91	14.75	3.84	315	0.000	14.48	0.00
2003	10.99	14.76	3.77	353	0.000	14.48	0.00
2004	11.08	14.77	3.68	388	0.000	14.48	0.00
2005	11.18	14.77	3.60	421	0.000	14.48	0.00
2006	11.29	14.78	3.50	453	0.000	14.48	0.00
2007	11.41	14.79	3.38	482	0.000	14.48	0.00
2008	11.54	14.80	3.28	510	0.000	14.48	0.00
2009	11.72	14.81	3.09	534	0.000	14.48	0.00
2010	11.91	14.82	2.91	557	0.000	14.48	0.00
2011	12.12	14.83	2.71	578	0.000	14.48	0.00
2012	12.37	14.85	2.47	596	0.000	14.48	0.00
2013	12.65	14.86	2.21	611	0.000	14.48	0.00
2014	12.95	14.88	1.93	624	0.000	14.48	0.00
2015	13.26	14.89	1.63	634	0.000	14.48	0.00
2016	13.60	14.91	1.31	641	0.000	14.48	0.00
2017	13.95	14.93	0.98	645	0.000	14.48	0.00
2018	14.30	14.95	0.65	648	0.000	14.48	0.00
2019	14.67	14.97	0.30	648	0.000	14.48	0.00
2020	15.03	14.99	-0.04	646	0.000	14.48	0.00
2021	15.38	15.01	-0.37	643	0.000	14.48	0.00
2022	15.70	15.03	-0.67	639	0.000	14.48	0.00
2023	16.03	15.05	-0.98	635	0.000	14.48	0.00
2024	16.33	15.07	-1.26	629	0.000	14.48	0.00
2025	16.62	15.09	-1.53	623	0.000	14.48	0.00
2026	16.89	15.10	-1.79	616	0.000	14.48	0.00
2027	17.14	15.12	-2.02	608	0.000	14.48	0.00
2028	17.38	15.14	-2.22	601	0.000	14.48	0.00
2029	17.55	15.15	-2.40	593	0.000	14.48	0.00
2030	17.71	15.17	-2.55	585	0.000	14.48	0.00
2031	17.86	15.18	-2.68	577	0.000	14.48	0.00
2032	17.99	15.19	-2.79	569	0.000	14.48	0.00
2033	18.09	15.20	-2.88	561	0.000	14.48	0.00
2034	18.16	15.21	-2.94	553	0.000	14.48	0.00
2035	18.19	15.22	-2.97	547	0.000	14.48	0.00
2036	18.21	15.23	-2.98	540	0.000	14.48	0.00
2037	18.22	15.23	-2.98	533	0.000	14.48	0.00
2038	18.21	15.24	-2.97	527	0.000	14.48	0.00
2039	18.19	15.24	-2.95	521	0.000	14.48	0.00
2040	18.17	15.25	-2.93	515	0.000	14.48	0.00
2041	18.16	15.25	-2.90	510	0.000	14.48	0.00
2042	18.15	15.26	-2.89	504	0.000	14.48	0.00
2043	18.14	15.26	-2.88	498	0.000	14.48	0.00
2044	18.14	15.26	-2.88	491	0.000	14.48	0.00
2045	18.15	15.27	-2.88	485	0.000	14.48	0.00
2046	18.16	15.27	-2.89	478	0.000	14.48	0.00
2047	18.18	15.28	-2.90	472	0.000	14.48	0.00
2048	18.20	15.28	-2.92	464	0.000	14.48	0.00
2049	18.24	15.29	-2.95	457	0.000	14.48	0.00
2050	18.28	15.29	-2.99	449	0.000	14.48	0.00
2051	18.33	15.30	-3.03	440	0.000	14.48	0.00
2052	18.40	15.31	-3.10	431	0.000	14.48	0.00
2053	18.48	15.31	-3.17	421	0.000	14.48	0.00
2054	18.56	15.32	-3.24	411	0.000	14.48	0.00
2055	18.64	15.33	-3.32	400	0.000	14.48	0.00
2056	18.73	15.33	-3.39	389	0.000	14.48	0.00
2057	18.81	15.34	-3.47	377	0.000	14.48	0.00
2058	18.90	15.35	-3.55	365	0.000	14.48	0.00
2059	18.98	15.36	-3.62	352	0.000	14.48	0.00
2060	19.05	15.36	-3.69	339	0.000	14.48	0.00
2061	19.12	15.37	-3.75	325	0.000	14.48	0.00
2062	19.19	15.38	-3.81	311	0.000	14.48	0.00
2063	19.25	15.38	-3.87	297	0.000	14.48	0.00
2064	19.31	15.39	-3.92	282	0.000	14.48	0.00
2065	19.37	15.39	-3.97	267	0.000	14.48	0.00
2066	19.42	15.40	-4.02	251	0.000	14.48	0.00
2067	19.47	15.40	-4.07	235	0.000	14.48	0.00
2068	19.53	15.41	-4.12	218	0.000	14.48	0.00
2069	19.58	15.41	-4.17	201	0.000	14.48	0.00
2070	19.63	15.42	-4.21	184	0.000	14.48	0.00
2071	19.68	15.42	-4.26	166	0.000	14.48	0.00
2072	19.73	15.42	-4.31	147	0.000	14.48	0.00
2073	19.79	15.43	-4.36	128	0.000	14.48	0.00
2074	19.83	15.43	-4.40	108	0.000	14.48	0.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	15.58	15.57	0.01	2.08

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback

Office of the Actuary
Social Security Administration
June 6, 1999

SOCIAL SECURITY ADMINISTRATION
April 16, 1999

Senator Phil Gramm

MEMORANDUM

Refer To: TCC

Subject: Preliminary Analysis of the Effects of The Social Security Preservation Act on OASDI Program Financing—INFORMATION

The attached tables provide a preliminary analysis of the plan reflecting the provisions outlined below. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

As described below, the plan would eliminate the long-range OASDI actuarial deficit, estimated at 2.07 percent of taxable payroll under present law. The OASDI trust fund would be substantial and rising at the end of the long-range 75-year period.

THE PLAN

The plan would establish SAFE Accounts beginning in the year 2000 with contributions equal to 3 percent of each worker's OASDI covered taxable earnings from the OASDI trust funds. An additional 2 percent of taxable earnings would be contributed from the OASDI trust funds for all workers who are age 35, 36, . . , 55 at the beginning of 2000. The OASDI trust funds would be reimbursed from General Fund of the Treasury, making use of the General Budget surplus that is currently projected.

SAFE Accounts would be established under regulation of a Board, with a maximum administrative expense of 0.3 percent of assets each year. It is not clear what discretion individuals would be allowed in selecting their portfolio allocation.

At retirement, SAFER-Annuity payments would be made from accounts that would continue to be invested as prior to retirement. Monthly payments from the SAFER Annuities would be determined at the time of OASDI benefit entitlement based on a CPI-indexed life-annuity calculation reflecting the account balance at that time, the existence of an eligible spouse or divorced spouse and any other family members who might potentially receive OASDI benefits in the future, and the "expected" future yield on the assets in the SAFER Annuity. Separate payments would be determined based on the accumulation of the 3-percent contributions and the accumulation of supplemental contributions of 2 percent for those ages 35–55 in 2000. The SAFER Annuity would make these payments, with adjustment for price inflation, for all individuals with potential OASDI benefits from the workers earnings. SAFER Annuities would also be limited to an administrative expense factor of 0.3 percent.

If an individual dies before retiring, with no potential survivor beneficiaries, the balance in the SAFE Annuity goes entirely to the worker's estate. Because SAFER Annuity payments are treated like life annuities, any remaining balance in the SAFER Annuity of an individual who dies prematurely remains in the SAFER fund to cover the expense of those who live longer than expected.

The Social Security program would offset (reduce) benefits by 80 percent of the amount paid from the 3-percent SAFER accumulation (and by 100 percent of the 2-percent SAFE Account accumulation), and guarantees that individual will receive lifetime payments from the SAFER Annuities and OASDI combined, that are at least equal to present law OASDI monthly benefits plus 20 percent of the calculated annuity-like payment from the 3-percent SAFER Annuity. Because the Social Security trust funds are the ultimate guarantee of benefit payments, it is critical that expected yields on SAFER Annuities not be overestimated.

The "recapture of corporate tax" on individual account yield would be directed to the OASDI trust funds. This recapture would be specified in law, intending to reflect the additional corporate taxes resulting from the additional domestic corporate investment from account assets. The plan would specify that the recapture would be assumed to equal 23.9 percent of the real, before tax, corporate return on investments. Because reported real yield on accounts would be after corporate tax, and the 23.9 percent rate is intended to apply to corporate income before tax, the actual rate applied to after tax income would be 31.4% = 23.9%/(1 − .239). This provision would provide a substantial and growing source of income to the OASDI program.

The reimbursement of the OASDI trust funds for the cost of SAFE Account investments would be permanently reduced in any year by as much as possible so that future expected OASDI tax income (including corporate tax recapture) would never fall below expected OASDI cost (reduced by benefit offset from the SAFER payments).

RESULTS

Table 1.0 illustrates the expected financing of OASDI assuming the SAFE Accounts and SAFER Annuities yield a real return of 5.5 percent on average, with an administrative expense of 0.3 percent. Under this assumption, an immediate reduction in the amount of reimbursement to the OASDI trust funds of 0.4 percentage point would be made in 2000. Additional reductions in reimbursements to the trust funds would commence in 2026, as the payroll tax required for OASDI would fall to 5.8 percent by 2066. By 2040, the payroll tax required for OASDI would be reduced by 3.5 percent, from 12.4 to 8.9 percent. With the full 12.4 percent payroll tax still in effect, the portion not needed for OASDI would effectively pay for the entire SAFE-Account contributions from that point forward. Further reductions in the payroll tax required for OASDI could be used to increase the size of the SAFE contribution after 2040.

Achieving the 5.5 percent real yield in the example above would require investment in 63 percent stock, with a real yield of 7 percent and 37 percent in long-term U.S. Government bonds with a real yield of 3 percent. Assuring that the average investor put this high a portion of the account in stock might require restriction on investment choice. Currently 401-K investments are invested only about 50 percent in stock, based on information obtained by the 1994–96 Advisory Council. However, because the Federal government would effectively share the risk of investing in SAFE Accounts and SAFER Annuities, many workers may opt for a more aggressive investment portfolio that in 401-K's.

If accounts were invested about 50 percent in stock, and 50 percent in U.S. Government bonds, the expected average real yield would be 5 percent, or 4.7 percent after administrative expense. Under this assumption the reimbursement to OASDI could be permanently reduced in 2000, but reductions would begin in 2028. reductions would total 3.1 percent by 2044, so that the cost of SAFE contributions would be covered by the payroll tax not credited to OASDI from that point forward. By 2060, the amount of the payroll tax rate required for OASDI would be expected to be 8.0 percent.

Table 3.0 illustrates that even if individual accounts were to achieve a real yield of only 3 percent (the expected real yield on U.S. Government bonds), 2.7 percent after administrative expense, the OASDI trust Funds would still be solvent for the long-range period, and the trust fund ratio would be relatively stable at the end of the period. However, the entire 12.4 percent payroll tax would continue to be required for the OASDI program.

STEPHEN C. GOSS
Deputy Chief Actuary

Attachments 02

Table 1.0	e Gramm 3% IA Contrib, 80%Offset, (+2% if 35-55 in2000/100%offse					IA Cntrb	3 %. Ben Offset	80.0 %
NO Clawback	With Ult Real TF Int Rate of		3.0	CorpTax toTF as%of Pre-			Remaining Surp to TF	0 %
at Death <65	With Ult Real IA Yld Rate of		5.2	tax IA RealYld 23.9				0 % BenCut
If No Survivor	With Annuity Net Yld Rate		5.2					

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.79	12.25	1.46	217	-0.40	12.00	4.22
2001	10.83	12.36	1.54	234		12.00	4.20
2002	10.91	12.44	1.53	251		12.00	4.17
2003	10.97	12.51	1.54	268		12.00	4.15
2004	11.05	12.57	1.52	283		12.00	4.12
2005	11.13	12.64	1.51	297		12.00	4.09
2006	11.23	12.71	1.48	311		12.00	4.04
2007	11.33	12.78	1.45	324		12.00	4.00
2008	11.44	12.86	1.42	336		12.00	3.96
2009	11.58	12.95	1.36	347		12.00	3.91
2010	11.74	13.04	1.30	357		12.00	3.86
2011	11.91	13.14	1.23	367		12.00	3.81
2012	12.10	13.24	1.14	377		12.00	3.75
2013	12.31	13.35	1.04	385		12.00	3.70
2014	12.52	13.45	0.93	393		12.00	3.65
2015	12.75	13.55	0.80	400		12.00	3.60
2016	12.98	13.65	0.66	406		12.00	3.55
2017	13.22	13.75	0.53	411		12.00	3.49
2018	13.46	13.85	0.40	415		12.00	3.45
2019	13.68	13.95	0.27	418		12.00	3.40
2020	13.89	14.05	0.16	421		12.00	3.36
2021	14.08	14.15	0.07	425		12.00	3.31
2022	14.21	14.24	0.03	429		12.00	3.27
2023	14.32	14.34	0.01	435		12.00	3.23
2024	14.41	14.43	0.02	441		12.00	3.20
2025	14.45	14.51	0.06	448		12.00	3.16
2026	14.46	14.50	0.04	457	-0.10	11.90	3.14
2027	14.43	14.57	0.14	467		11.90	3.11
2028	14.36	14.44	0.09	480	-0.20	11.70	3.09
2029	14.24	14.51	0.27	493		11.70	3.07
2030	14.07	14.07	0.00	511	-0.50	11.20	3.06
2031	13.87	14.12	0.25	527		11.20	3.05
2032	13.80	13.88	0.08	542	-0.30	10.90	3.04
2033	13.69	13.94	0.25	557		10.90	3.04
2034	13.54	13.59	0.05	575	-0.40	10.50	3.03
2035	13.37	13.64	0.28	594		10.50	3.03
2036	13.16	13.19	0.02	616	-0.50	10.00	3.02
2037	12.95	13.23	0.28	638		10.00	3.02
2038	12.71	12.77	0.06	664	-0.50	9.50	3.01
2039	12.47	12.80	0.34	690		9.50	3.01
2040	12.21	12.23	0.03	721	-0.60	8.90	3.00
2041	11.98	12.26	0.30	750		8.90	3.00
2042	11.73	11.79	0.06	782	-0.50	8.40	3.00
2043	11.51	11.82	0.30	812		8.40	3.00
2044	11.31	11.34	0.03	846	-0.50	7.90	3.00
2045	11.12	11.37	0.25	876		7.90	3.00
2046	10.94	10.99	0.05	910	-0.40	7.50	3.00
2047	10.78	11.02	0.23	942		7.50	3.00
2048	10.63	10.64	0.00	976	-0.40	7.10	3.00
2049	10.50	10.66	0.16	1008		7.10	3.00
2050	10.39	10.48	0.09	1041	-0.20	6.90	3.00
2051	10.29	10.50	0.21	1073		6.90	3.00
2052	10.21	10.22	0.01	1106	-0.30	6.60	3.00
2053	10.14	10.24	0.10	1135		6.60	3.00
2054	10.09	10.16	0.07	1166	-0.10	6.50	3.00
2055	10.03	10.17	0.15	1197		6.50	3.00
2056	9.97	9.99	0.01	1229	-0.20	6.30	3.00
2057	9.92	10.00	0.08	1261		6.30	3.00
2058	9.87	9.91	0.04	1294	-0.10	6.20	3.00
2059	9.82	9.92	0.10	1327		6.20	3.00
2060	9.76	9.83	0.06	1362	-0.10	6.10	3.00
2061	9.71	9.83	0.12	1399		6.10	3.00
2062	9.65	9.73	0.08	1436	-0.10	6.00	3.00
2063	9.61	9.73	0.12	1472		6.00	3.00
2064	9.55	9.63	0.07	1511	-0.10	5.90	3.00
2065	9.51	9.62	0.12	1550		5.90	3.00
2066	9.47	9.52	0.05	1589	-0.10	5.80	3.00
2067	9.43	9.51	0.09	1629		5.80	3.00
2068	9.40	9.50	0.11	1668		5.80	3.00
2069	9.37	9.49	0.12	1707		5.80	3.00
2070	9.35	9.48	0.13	1746		5.80	3.00
2071	9.34	9.47	0.13	1785		5.80	3.00
2072	9.34	9.46	0.12	1823		5.80	3.00
2073	9.33	9.45	0.11	1862		5.80	3.00
2074	9.38	9.43	0.05	1888		5.80	3.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI
1999 -2073	12.01	13.04	1.03

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback
** Including Transfer for Corp Income Tax

Office of the Actuary
Social Security Administration
April 16, 1999

Table 2.0	a Gramm 3% IA Contrib, 80%Offset, (+2% if 35-55 in2000/100%offse				IA Cntrb	3 %, Ben Offset	80.0 %
NO Clawback	With Ult Real TF Int Rate of		3.0	CorpTax toTF as%of Pro-		Remaining Surp to TF	0 %
at Death <65	With Ult Real IA Yld Rate of		4.7	tax IA RealYld 23.9	Change		0 % BenCut
If No Survivor	With Annuity Net Yld Rate		4.7		in OASDI	OASDI	IA
	Cost	Income	Annual	TFR	Contrib	Contrib	Contrib
Year	Rate*	Rate**	Balance	1-1-yr	Rate	Rate	Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.79	12.65	1.86	217		12.40	4.22
2001	10.83	12.75	1.93	236		12.40	4.20
2002	10.91	12.82	1.92	259		12.40	4.17
2003	10.97	12.89	1.91	278		12.40	4.15
2004	11.05	12.94	1.88	297		12.40	4.12
2005	11.13	13.00	1.87	315		12.40	4.09
2006	11.23	13.06	1.83	331		12.40	4.04
2007	11.33	13.12	1.79	347		12.40	4.00
2008	11.44	13.19	1.76	363		12.40	3.96
2009	11.59	13.27	1.68	376		12.40	3.91
2010	11.74	13.35	1.61	389		12.40	3.86
2011	11.91	13.44	1.53	402		12.40	3.81
2012	12.10	13.53	1.42	414		12.40	3.75
2013	12.31	13.62	1.31	424		12.40	3.70
2014	12.53	13.71	1.18	434		12.40	3.65
2015	12.76	13.80	1.03	443		12.40	3.60
2016	13.01	13.88	0.88	450		12.40	3.55
2017	13.25	13.97	0.72	456		12.40	3.49
2018	13.48	14.06	0.57	462		12.40	3.45
2019	13.72	14.14	0.42	466		12.40	3.40
2020	13.94	14.23	0.28	470		12.40	3.36
2021	14.14	14.31	0.17	475		12.40	3.31
2022	14.29	14.39	0.10	480		12.40	3.27
2023	14.42	14.47	0.05	485		12.40	3.23
2024	14.52	14.54	0.02	492		12.40	3.20
2025	14.59	14.62	0.03	499		12.40	3.16
2026	14.62	14.68	0.06	508		12.40	3.14
2027	14.62	14.75	0.12	518		12.40	3.11
2028	14.58	14.61	0.02	531	-0.20	12.20	3.09
2029	14.49	14.66	0.17	544		12.20	3.07
2030	14.36	14.40	0.04	561	-0.30	11.90	3.06
2031	14.21	14.45	0.24	578		11.90	3.05
2032	14.16	14.19	0.03	592	-0.30	11.60	3.04
2033	14.09	14.24	0.15	607		11.60	3.04
2034	13.98	13.98	0.00	624	-0.30	11.30	3.03
2035	13.83	14.02	0.18	642		11.30	3.03
2036	13.67	13.75	0.08	663	-0.30	11.00	3.02
2037	13.49	13.79	0.29	684		11.00	3.02
2038	13.30	13.31	0.02	709	-0.50	10.50	3.01
2039	13.09	13.34	0.25	734		10.50	3.01
2040	12.88	12.98	0.08	762	-0.40	10.10	3.00
2041	12.68	12.99	0.31	789		10.10	3.00
2042	12.49	12.51	0.02	819	-0.50	9.60	3.00
2043	12.32	12.53	0.21	846		9.60	3.00
2044	12.15	12.25	0.09	875	-0.30	9.30	3.00
2045	12.01	12.27	0.26	904		9.30	3.00
2046	11.87	11.88	0.01	934	-0.40	8.90	3.00
2047	11.75	11.90	0.15	963		8.90	3.00
2048	11.64	11.72	0.08	992	-0.20	8.70	3.00
2049	11.55	11.74	0.19	1021		8.70	3.00
2050	11.47	11.55	0.08	1050	-0.20	8.50	3.00
2051	11.41	11.57	0.16	1078		8.50	3.00
2052	11.38	11.39	0.02	1105	-0.20	8.30	3.00
2053	11.33	11.40	0.07	1130		8.30	3.00
2054	11.31	11.32	0.01	1157	-0.10	8.20	3.00
2055	11.28	11.33	0.05	1183		8.20	3.00
2056	11.25	11.35	0.08	1209	0.00	8.20	3.00
2057	11.24	11.36	0.11	1236		8.20	3.00
2058	11.22	11.27	0.04	1265	-0.10	8.10	3.00
2059	11.20	11.28	0.07	1293		8.10	3.00
2060	11.18	11.18	0.01	1322	-0.10	8.00	3.00
2061	11.15	11.19	0.04	1352		8.00	3.00
2062	11.13	11.19	0.06	1383		8.00	3.00
2063	11.11	11.20	0.09	1413		8.00	3.00
2064	11.08	11.20	0.11	1446		8.00	3.00
2065	11.06	11.20	0.14	1479		8.00	3.00
2066	11.05	11.20	0.15	1512		8.00	3.00
2067	11.03	11.19	0.17	1546		8.00	3.00
2068	11.02	11.19	0.18	1580		8.00	3.00
2069	11.01	11.19	0.18	1614		8.00	3.00
2070	11.01	11.18	0.17	1648		8.00	3.00
2071	11.01	11.18	0.17	1683		8.00	3.00
2072	11.02	11.18	0.15	1717		8.00	3.00
2073	11.03	11.17	0.13	1751		8.00	3.00
2074	11.08	11.16	0.08	1776		8.00	3.00
	Summarized						
	CostRt	IncRt	ActBal				
1999	OASDI	OASDI	OASDI				
-2073	12.46	13.60	1.14				

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback
** Including Transfer for Corp Income Tax

Office of the Actuary
Social Security Administration
April 16, 1999

Table 3.0 a Gramm 3% IA Contrib, 80%Offset, (+2% if 35-55 in2000/100%offse IA Cntrb 3 %, Ben Offset 80.0 %
NO Clawback With Ult Real TF Int Rate of 3.0 CorpTax toTF as%of Pre- Remaining Surp to TF 0 %
at Death <65 With Ult Real IA Yld Rate of 2.7 tax IA RealYld 23.9 0 % BenCut
If No Survivor With Annuity Net Yld Rate 2.7

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.79	12.65	1.86	217		12.40	4.22
2001	10.83	12.72	1.89	238		12.40	4.20
2002	10.91	12.75	1.85	258		12.40	4.17
2003	10.97	12.79	1.82	277		12.40	4.15
2004	11.06	12.81	1.76	295		12.40	4.12
2005	11.13	12.85	1.71	312		12.40	4.09
2006	11.23	12.88	1.65	327		12.40	4.04
2007	11.33	12.91	1.58	341		12.40	4.00
2008	11.45	12.95	1.50	355		12.40	3.96
2009	11.60	12.99	1.39	366		12.40	3.91
2010	11.76	13.04	1.28	375		12.40	3.86
2011	11.93	13.09	1.15	386		12.40	3.81
2012	12.14	13.14	1.00	394		12.40	3.76
2013	12.36	13.19	0.83	401		12.40	3.70
2014	12.60	13.24	0.65	407		12.40	3.65
2015	12.84	13.29	0.44	411		12.40	3.60
2016	13.11	13.33	0.22	413		12.40	3.55
2017	13.37	13.37	0.00	414		12.40	3.49
2018	13.64	13.42	-0.22	413		12.40	3.45
2019	13.91	13.46	-0.45	411		12.40	3.40
2020	14.18	13.50	-0.67	407		12.40	3.36
2021	14.42	13.54	-0.88	404		12.40	3.31
2022	14.63	13.58	-1.04	399		12.40	3.27
2023	14.82	13.62	-1.20	395		12.40	3.23
2024	14.99	13.65	-1.34	390		12.40	3.20
2025	15.14	13.68	-1.45	385		12.40	3.16
2026	15.26	13.71	-1.54	380		12.40	3.14
2027	15.35	13.74	-1.61	375		12.40	3.11
2028	15.41	13.76	-1.65	371		12.40	3.09
2029	15.44	13.78	-1.65	367		12.40	3.07
2030	15.43	13.80	-1.63	363		12.40	3.06
2031	15.40	13.82	-1.59	360		12.40	3.05
2032	15.45	13.84	-1.62	355		12.40	3.04
2033	15.48	13.85	-1.62	351		12.40	3.04
2034	15.47	13.87	-1.60	347		12.40	3.03
2035	15.43	13.88	-1.54	344		12.40	3.03
2036	15.37	13.89	-1.47	342		12.40	3.02
2037	15.30	13.90	-1.39	340		12.40	3.02
2038	15.22	13.91	-1.30	339		12.40	3.01
2039	15.13	13.92	-1.21	339		12.40	3.01
2040	15.03	13.93	-1.11	340		12.40	3.00
2041	14.95	13.93	-1.01	341		12.40	3.00
2042	14.87	13.94	-0.93	342		12.40	3.00
2043	14.81	13.94	-0.88	344		12.40	3.00
2044	14.75	13.95	-0.80	346		12.40	3.00
2045	14.71	13.96	-0.75	349		12.40	3.00
2046	14.67	13.96	-0.71	351		12.40	3.00
2047	14.64	13.97	-0.67	354		12.40	3.00
2048	14.63	13.98	-0.65	357		12.40	3.00
2049	14.62	13.99	-0.64	360		12.40	3.00
2050	14.63	13.99	-0.63	362		12.40	3.00
2051	14.65	14.00	-0.65	365		12.40	3.00
2052	14.68	14.01	-0.67	367		12.40	3.00
2053	14.73	14.02	-0.71	369		12.40	3.00
2054	14.78	14.03	-0.75	370		12.40	3.00
2055	14.83	14.04	-0.79	371		12.40	3.00
2056	14.88	14.04	-0.84	372		12.40	3.00
2057	14.93	14.05	-0.88	373		12.40	3.00
2058	14.98	14.06	-0.92	373		12.40	3.00
2059	15.03	14.07	-0.98	373		12.40	3.00
2060	15.08	14.08	-1.00	373		12.40	3.00
2061	15.12	14.08	-1.04	373		12.40	3.00
2062	15.16	14.09	-1.07	373		12.40	3.00
2063	15.19	14.09	-1.10	373		12.40	3.00
2064	15.23	14.10	-1.13	372		12.40	3.00
2065	15.26	14.10	-1.16	371		12.40	3.00
2066	15.29	14.11	-1.19	370		12.40	3.00
2067	15.32	14.11	-1.21	369		12.40	3.00
2068	15.36	14.11	-1.24	368		12.40	3.00
2069	15.39	14.12	-1.27	367		12.40	3.00
2070	15.43	14.12	-1.30	365		12.40	3.00
2071	15.46	14.13	-1.34	363		12.40	3.00
2072	15.50	14.13	-1.37	361		12.40	3.00
2073	15.54	14.13	-1.41	359		12.40	3.00
2074	15.58	14.13	-1.45	355		12.40	3.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI
1999 -2073	13.78	14.02	0.24

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback
** Including Transfer for Corp Income Tax

Office of the Actuary
Social Security Administration
April 16, 1999

SOCIAL SECURITY ADMINISTRATION
January 13, 1999

Harry C. Ballantyne
Chief Actuary

MEMORANDUM

Refer To: TCC

Subject: Estimates of Long-Range OASDI Financial Effect of a Possible Modification of The Social Security Solvency Act of 1998, Proposed by Senator Moynihan—INFORMATION

This memorandum provides long-range estimates, based on the intermediate assumptions of the 1998 Trustees Report, for a possible modification under consideration for The Social Security Solvency Act of 1998 (S.1792), proposed by Senators Moynihan and Kerrey. This analysis has been produced at the request of David Podoff of Senator Moynihan's staff. An earlier memorandum, dated March 4, 1998, provides long-range estimates of S.1792, based on the intermediate assumptions of the 1997 Trustees Report.

The possible modification of the comprehensive proposal is described in Table A, attached. For each individual provision and for the total proposed package, Table A provides the following estimates:

- The change, from present law, in the long-range OASDI actuarial balance.
- The change, from present law, in the OASDI annual income rate in 2070.
- The change, from present law, in the OASDI annual cost rate in 2070.
- The change, from present law, in the OASDI annual balance in 2070.

If all modifications are implemented and tax rates are changed as shown in Table A (including the 1 percentage point reduction in COLA), the resulting long-range actuarial balance for the 75-year period (1998–2072) is estimated to be +0.03 percent of taxable payroll. The trust fund ratio (ratio of trust fund assets to annual outgo) would increase from 171 percent as of the beginning of 1998 to 286 percent as of the beginning of 2014. The trust fund ratio would then decrease to 130 percent as of the beginning of 2035. For the remaining period of the long-range projection period (2036–2072), the fund ratio would stay relatively stable (between 128 and 135).

Table A. Estimated Long-Range OASDI Financial Effect of Possible Modification to S.1792 (Moynihan/Kerrey)

Estimated Change in Annual Measures: 2070

Provision	Actuarial Balance (75-year)	Income Rate	Cost Rate	Annual Balance
1 For 1999 and later, reduce the OASDI automatic cost of living adjustment (COLA) by 1.0 percentage point.	1.44	−0.12	−2.43	2.31
2 Subject OASDI benefits to income tax in a manner similar to that prescribed for benefits received from private and government employee defined benefit pension plans, with all current thresholds levels for taxing OASDI benefits eliminated. This provision is phased in over the period 2000–2004.	0.40	0.22	0.00	0.22
3 Extend OASDI coverage to all State and local government employees hired after 2001.	0.21	0.00	−0.02	0.02
4 Increase maximum computation period from 35 years to 38 years for retirement, survivor, and disability (death or disability entitlement at age 62 or higher). The computation period would increase to 36 years for those first eligible in 2002, 37 years for those first eligible in 2003, and 38 years for those first eligible after 2003.	0.25	−0.02	−0.44	0.41
5 Retain the normal retirement age (NRA) at age 65. Multiply all benefit formula factors (90, 32, and 15) by 0.988 for 2000–2017 and by 0.997 for 2018–2065. The resulting factors for beneficiaries age 62 in 2065 are 62.70, 22.29, and 10.45. Disability and young survivor beneficiaries maintain the current formula factors. (Details concerning the calculation of benefits for the disabled and aged widows are being developed.)	0.70	−0.12	−1.81	1.69
6 Effective 1/1/2003, eliminate the retirement earnings test for beneficiaries age 62 and older.	0.01	−0.01	−0.28	0.27
7 Raise the OASDI contribution and benefit base to $87,000 in 2002, $94,000 in 2003, and $99,900 in 2004. After 2004, resume indexing the contribution and benefit base using the average wage index.	0.24	−0.01	−0.25	0.24
Total for Provisions 1 through 7 (adjusted to take account of interactions)	2.95	−0.11	−4.68	4.57
8 Change the OASI and DI payroll tax beginning in 2000 as follows (adjusted to take account of interactions): 11.4% for years 2000–2001; 10.4% for years 2002–2029; 12.4% for years 2030–2034; 12.9% for years 2035–2049; 13.3% for years 2050–2059; 13.7% for years 2060+	−0.73	1.30	0.00	1.30
Total for Provisions 1 through 8 (adjusted to take account of interactions)	2.22	1.19	−4.68	5.87

Based on the intermediate assumptions of the 1998 Trustees Report under present law, the long-range actuarial balance for the 75-year period (1998–2072) is estimated to be −2.19 percent of taxable payroll. For 2070, the annual income rate, annual cost rate, and annual balance are 13.34, 19.54, and −6.20 respectively.

[1] The indicated effect on the Actuarial Balance is for a legislative change that would reduce the COLA by this amount. If instead, the COLA is reduced by this amount, on average, as a result of technical changes in the CPI by the BLS, the effect on the Actuarial Balance may be smaller because of potential related changes in other economic parameters.

[2] This provision is assumed to achieve the same cost effect as gradually increasing the normal retirement age (NRA) to age 70 as in S.1792.

Office of the Actuary, Social Security Administration, January 13, 1999

SOCIAL SECURITY ADMINISTRATION
June 3, 1999

Harry C. Ballantyne
Chief Actuary

MEMORANDUM

Refer To: TCC

Subject: Estimated Long-Range OASDI Financial Effects of a Bipartisan Social Security Proposal—INFORMATION

This memorandum provides estimates of the effect on the financial status of the OASDI program of a plan developed by Senators Gregg, Breaux, Kerrey (B), and Grassley. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

LONG-RANGE FINANCIAL EFFECTS

The plan would improve the OASDI actuarial balance by an estimated 2.35 percent of taxable payroll, eliminating the actuarial deficit of 2.07 percent of taxable payroll under present law and resulting in a positive actuarial balance of about 0.28 percent of taxable payroll. The level of OASDI trust fund assets as a percentage of annual OASDI cost (the trust fund ratio) would be expected to decline after reaching 252 percent in 2014, to a low point of 104 percent at the beginning of 2041. The trust fund ratio would rise after 2041, reaching a level of 505 percent at the end of the long-range (75-year) period, at which point the trust fund ratio would be rising by about 20 percentage points each year. Table 2, attached, provides estimated annual cost rates, annual income rates, annual balances, as well as annual trust fund ratios.

DESCRIPTION OF PROVISIONS

As shown in the attached Table 1, the plan consists of 13 provisions.

Provision 1 would create a new PIA bend point between the current two bend points, splitting the PIA bracket where the 32-percent PIA factor currently applies in two. Rather than 32 percent, PIA factors of 70 and 20 would apply above and below the new bend point within this bracket. The PIA factor of 15 percent would be replaced with 10 percent above the top bend point. This provision would be phased in gradually between 2006 and 2015, and is designed to have no net effect on the long-range cost of the OASDI program.

Provision 2a would eliminate the 11-year hiatus between the increase in the normal retirement age (NRA) from 65 to 66 (2000–05) and the increase from 66 to 67 (2017–22). The NRA would thus be increased by 2 months per year beginning 2000 until the NRA of 67 is reached for individuals attaining age 62 in 2011 and later.

Provision 2b would change the early retirement factors and delayed retirement credits in an attempt to reflect the fact that the marginal increase in the full (PIA) benefit level for earnings after reaching retirement age is, generally, relatively small. (Reduction and increment factors provided under current law are intended to provide actuarially equivalent lifetime benefits payable at different starting ages for a fixed earnings history.) This relatively small marginal increase results from the weighted PIA benefit formula, which provides a larger marginal amount of benefit per dollar of AIME for low, or early-in-career, earnings. This provision is intended to eliminate the marginal disincentive to work past EEA that is provided by the weighting in the PIA formula. Because the extent of this marginal effect depends upon the level of earnings a worker has had in earlier years, no absolute adjustment can be provided that would be appropriate for all workers. Rough estimates of adjustments to the reduction and increment factors have thus been used.

The chart below displays the proposed monthly early retirement reductions that are applicable for retired worker beneficiaries for the first 36 months for which benefits are received prior to NRA under both current law and the provision. (Different factors apply to aged spouse beneficiaries and aged widow beneficiaries.)

Similar increases for aged spouse beneficiaries would be applied, increasing the monthly reduction for the first 36 months of entitlement before NRA from 25/36 percent under present law to 30/36 percent under the provision.

Monthly Reduction in Benefits for Each of First 36 Months of Retirement Before NRA

Age 62 in:	2001	2002	2003	2004	2005	2006+
Present Law	20/36%	20/36%	20/36%	20/36%	20/36%	20/36%
Proposal	20/36%	21/36%	22/36%	23/36%	24/36%	25/36%

The reductions that are proposed for the fourth and fifth year before NRA are 12/24% per month (current law reductions are 10/24% per month) for both retired worker and aged spouse beneficiaries. The reductions for the fourth and fifth year before NRA are applicable to all new eligibies who reach age 62 after 1999.

The delayed retirement credit (DRC) under present law is scheduled to increase to 8% per year for workers attaining age 65 after 2007. The DRC would continue to increase at the rate of 0.5 percentage point every two years, with the first increase applied to those attaining age 65 in 2010. An ultimate factor of 10 percentage points per year is reached for workers reaching 65 after 2015. The delayed retirement credit applies for months for which retired worker benefits are not received between NRA and age 70.

The ultimate percentages of PIA payable for retired workers by age at initial benefit entitlement are shown below.

Ultimate Percent of PIA Payable for Retired Worker Beneficiaries by Age at Initial Entitlement to Benefits

Age at Initial Entitlement:	NRA–5	NRA–4	NRA–3	NRA–2	NRA–1	NRA
Present Law	70%	75%	80%	86.7%	93.3%	100%
Proposal	63%	69%	75%	83.3%	91.7%	100%

The percentage of PIA payable for non-disabled aged widow beneficiaries newly eligible at age 60 would remain at 71.5 percent. The percentages payable for those newly eligible at ages between 60 and the NRA would scale linearly between 71.5 and 100 percent, as under present law.

Provision 3 would gradually reduce the size of all of the PIA factors in a manner that would roughly approximate the effect of continuing the increase in the NRA at 2 months per year to age 68, with indexing thereafter to an NRA of 70 by 2065. Rather than modifying the NRA, the provision would reduce each of the PIA factors (90, 32, 15 under current law, and 90, 70, 20, 10 after provision 1) by 1.2 percent (multiply by 0.988) each year 2012–17, and by 0.03 percent (multiply by 0.997) each year 2018 through 2065.

The PIA factors would ultimately be reduced by about 19.5 percent under this provision, from levels of 90, 32, 15 to levels of 72.47, 25.77, 12.08, under current law, or from 90, 70, 20, 10 to levels of 72.47, 56.36, 16.10, 8.05 after provision 1. The modified PIA would apply to benefits payable for most retired worker, aged spouse, and aged surviving spouse beneficiaries. The current-law, unmodified PIA formula would apply for disabled worker beneficiaries, and to retirement benefits payable to disabled workers converted to retirement status at NRA (and their dependents).

Provision 4 would gradually increase the PIA benefit computation period for retired workers from 35 to 40 years, except for the lower earner of a married couple. The provision would also allow the inclusion of earnings of all years in the numerator of the AIME, even if the number of years with earnings exceeds 40.

This provision would apply in determining benefits for retired worker and their dependents and for survivors of deceased workers. This provision does not apply in determining benefits for disabled workers and their dependents.

In calculating the AIME for a retired worker under present law, the highest 35 years of indexed earnings are used in determining the numerator of the AIME and a benefit computation period of 35 years is used in determining the denominator. Under this provision, the following changes are made in the calculation of the AIME for someone newly eligible for retirement benefits after 2001.

• The number of years of earnings, used in calculating the numerator of the AIME, is gradually increased, reaching all years of earnings in 2010.

• The benefit computation period, used in determining the denominator of the AIME, is gradually increased, reaching 40 years (5 additional years), except for the lower earner of a married couple. In the case of a two-earner couple, the benefit computation period for the earner with the lower PIA is 35 years.

The chart below indicates the phase in schedule of the above changes.

Change in Calculation of AIME for Retired Worker

(assumes the retired worker is not the lower earner of a married couple)

Newly Eligible in Years:	2002–2003	2004–2005	2006–2007	2008–2009	2010+
Present Law					
Years in Numerator	35	35	35	35	35
Denominator (in years	35	35	35	35	35
Proposal					
Years in Numerator	37	39	41	43	all
Denominator (in years	36	37	38	39	40

[1] Years in Numerator: Refers to the number of years of earnings used in calculating the numerator of the AIME.
[2] Denominator (in years): Refers to the benefit computation period (in years) used in calculating the denominator of the AIME.

Under this provision alone, the number of benefit computation years used for the denominator of the AIME for a retired worker turning age 62 after 2009 would be 40. Under current law, the number of benefit computation years is determined by subtracting 5 dropout years from the number of elapsed years (years age 22 through the year prior to reaching EEA). Under this proposed provision, the increase in the number of benefit computation years would be accomplished by reducing the number of dropout years, ultimately to zero. In addition, each year, except for 2010, that the number of dropout years is reduced by one year, the number of years of earnings, used in calculating the numerator of the AIME, is increased an additional two years. In 2010, all years of earnings are used in calculating the numerator of the AIME for someone newly eligible for retirement or survivor benefits.

Provision 5 would redirect to the OASDI trust funds the revenue from taxation of OASDI benefits that is currently transferred to the Medicare HI trust fund. Revenue collected by the IRS from Federal income taxes payable on OASDI benefits, in excess of the tax on 50 percent of such benefits, would be redirected from the Medicare HI trust fund to the OASDI trust funds. The provision would redirect 10 percent of this revenue for 2005, 20 percent for 2006, ... , and 100 percent for 2014 and later.

Provision 6 would eliminate the retirement earnings test for beneficiaries age 62 and above, effective in 2003.

Provision 7 would increase the indexing of the OASDI benefit and contribution base (the taxable maximum) to keep the percent of OASDI covered earnings that is taxable at 86 percent. Under current indexing, the percent taxable is projected to fall below 85 percent for 2008 and later.

Provision 8 would reduce the OASDI cost-of-living adjustment (COLA) to the measured increase in the CPI–W less 0.5 percentage point for December 2000 and later. The reduced COLA would apply only to beneficiaries newly eligible for OASDI benefits after 1999.

Provision 9 would gradually implement an option for the surviving spouse of a married couple to receive up to 75 percent of the benefit that would be payable to the couple if they were still both alive. The percentage of the couple benefit payable under the option would be 51 percent for surviving spouses newly eligible in 2002 or 2003, 52 percent for those newly eligible in 2004 or 2005, ..., and 75 percent for those newly eligible in 2050 and later. eligibility for the option occurs when the survivor and the deceased spouse, if still alive, would both be eligible for a retired worker or aged spouse benefit. The benefit under the option would be limited to the retired worker benefit that would be payable to the survivor if he/she had had earnings at the level of the OASDI contribution and benefit base from age 22 through 61, with the retired worker benefit reduced as of the age at first actual entitlement to either retired worker, aged spouse, or aged surviving spouse benefit (but not less than 62).

Provision 10 would redirect 2 percentage points of the OASDI payroll tax to individual accounts for all covered workers beginning 2000. OASDI retirement (including converted disabled workers after reaching NRA) and aged survivor benefits payable on the accounts of individuals with redirected taxes would be reduced in the future.

The benefit reduction would be based on a hypothetical accumulation of the amount of taxes redirected to the individual account, using the yield rates on special government bonds held by the trust funds, up to the point of entitlement to retirement benefits. At that point, the ratio of the value of the hypothetical accumulated account to the present value of all benefits expected to be paid on the worker's ac-

count would be calculated. Future OASDI benefits paid on the workers account would then be reduced by this ratio.

Income tax on the amount of the reduction in OASDI benefits from this provision would be assessed against the accumulated account of the worker. No other assessment (clawback) against the individual account would be made for the benefit of the OASDI trust funds at death.

Provision 11 provides a transfer to the OASDI trust funds from the General Fund of the Treasury increasing from 0.6 percent of OASDI effective taxable payroll in 2000, to 0.8 percent in 2020, 1.0 percent in 2040, and 1.2 percent in 2060. This transfer is intended to "recapture" the gains from lowering the CPI-indexing of income tax brackets by 0.5 percentage point in 2000 and later.

Provision 12 would add a General Revenue contribution to the individual accounts of workers with low earnings. However the additional contributions would not be included in the calculation of the OASDI benefit reduction in provision 10.

Provision 13 would provide for a $1,000 contribution at birth to the individual accounts of each person born in the United States in 2000 and later. An additional $500 would be deposited into accounts at attainment of each age 1 through 5. These amounts would be indexed by the SSA average wage indexing series after 2000. Contributions would be made from the General Fund of the Treasury. One half of the contributions at ages 0 through 5 would be included in the calculation of OASDI benefit reduction in provision 10.

STEPHEN C. GOSS
Deputy Chief Actuary
ALICE H. WADE
Actuary

Attachments

Table 1. Estimated Long-Range OASDI Financial Effect of Reform Proposal

	Provision	Estimated Change in Long-range OASDI Actuarial Balance (percent of taxable payroll)
1	Establish a new bend point in the PIA formula equal to 197.5% of the present law first bend point. PIA formula factors would be initially set at 0.90, 0.32, 0.32, and 0.15 (yielding the same benefit as current law). Beginning with new eligibles in 2006, the second formula factor would be increased each year by .038, the third formula factor would be decreased each year by .012, and the fourth formula factor would be decreased each year by 0.005, until reaching factors of 0.90, 0.70, 0.20, and 0.10 for newly eligibles in 2015 and later.	1
2a	Eliminate the NRA hiatus between 66 and 67. NRA reaches 67 for those attain 62 in 2011.	0.15
2b	Increase the size of early retirement factors between 2002 and 2006 and delayed retirement credits between 2010 and 2016. This provision reflects interaction with provision 2a.	0.33
3	Multiply all benefit formula factors (90, 32, and 15) by 0.988 for 2012–2017 and by 0.997 for 2018–2065. The resulting factors for beneficiaries age 62 in 2065 are 72.47, 25.77, and 12.08. The present law formula factors are maintained in determining benefits for disability beneficiaries and retired worker beneficiaries who convert from disability.	0.74
4	Increase the benefit computation period by up to 5 additional years for new eligibles (by one additional year for new eligibles in each year 2002, 04, 06, 08, 10). For two-earner couples, however, cap the benefit computation period for the earner with the lower PIA at 35 years. In conjunction with increasing the benefit period, phase in including earnings for all years in calculating the AIME.	0.19
5	Credit all revenue from taxation of OASDI benefits to the OASDI trust funds by 2014 (phase revenue from HI to OASDI during the period 2005–2014).	0.32
6	Effective 1/1/2003, eliminate the retirement earnings test for individuals who are 62 or older.	....

Table 1. Estimated Long-Range OASDI Financial Effect of Reform Proposal—Continued

	Provision	Estimated Change in Long-range OASDI Actuarial Balance (percent of taxable payroll)
7	Maintain the benefit and contribution base at a level so that 86 percent of covered earnings are taxable.	0.18
8	Reduce the OASDI COLA by 0.5 percent for beneficiaries newly eligible in 2000 and later.	0.65
9	Beginning with newly eligible aged surviving spouses in 2002, gradually (over a 49-year phase in period) provide a minimum benefit equal to 75-percent of the combined benefits payable if both were still alive. −0.10.	
	Total for Provisions 1 through 9 (including interactions among provisions) ..	2.18
10	Beginning in 2000, redirect 2 percentage points of the OASDI payroll tax to individual accounts. Reduce OASDI benefits based on the accumulation of these accounts at the interest rate earned by the OASDI Trust Funds. No "clawback" of account balance at death.	-.62
11	Transfer from General Revenue to the OASDI Trust Fund the following amounts, expressed as a percent of taxable payroll: 0.6% each year 2000–2019, 0.8% each year 2020–2039, 1.0% each year 2040–2059, and 1.2% each year after 2059.	0.78
12	Additional General Revenue contribution to the individual account of low income workers.	....
13	For every individual born after 1999, deposit money during the first five years of life into individual accounts from General Revenue. The amount of money for the year 2000 would be $1000 during the first year of life and $500 in each of the next five years. After 2000, the dollar amounts would be increased by the increase in wages. Half of the accumulated value of these deposits (at the trust fund interest rate) would be used to offset OASDI benefits.	0.01
	Total for Provisions 1 through 13 (including interactions among provisions)	2.35

[1] Negligible (between −0.005 and .005 percent of payroll) change in the OASDI long-range actuarial balance.

Based on the intermediate assumptions of the 1999 Trustees Report under present law, the long-range actuarial balance for the 75-year period (1999–2073) is −2.07 percent of taxable payroll.

June 3, 1999 Social Security Administration Office of the Chief Actuary

Gregg.Breaux 6/3 Memo
Table 2 a Gregg.Breaux.Kerrey, Grassley--Provisions 1-13 IA Cntrb 2 %, Ben Offset 100.0 %
NO Clawback at Death
With Ult Real TF Int Rate of 3.0
With Ult Real IA Yld Rate of 3
With Annuity Net Yld Rate 3

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.81	12.70	1.89	193		12.40	0
2000	10.74	11.25	0.50	216	-1.40	11.00	2.00
2001	10.88	11.28	0.40	223		11.00	2.00
2002	10.92	11.28	0.35	229		11.00	2.00
2003	11.18	11.29	0.11	230		11.00	2.00
2004	11.20	11.29	0.10	233		11.00	2.00
2005	11.20	11.31	0.11	236		11.00	2.00
2006	11.22	11.34	0.12	239		11.00	2.00
2007	11.23	11.36	0.13	241		11.00	2.00
2008	11.25	11.39	0.14	244		11.00	2.00
2009	11.31	11.41	0.10	246		11.00	2.00
2010	11.38	11.45	0.07	248		11.00	2.00
2011	11.46	11.48	0.02	250		11.00	2.00
2012	11.57	11.51	-0.06	251		11.00	2.00
2013	11.69	11.54	-0.15	251		11.00	2.00
2014	11.82	11.57	-0.24	252		11.00	2.00
2015	11.95	11.59	-0.36	251		11.00	2.00
2016	12.08	11.61	-0.47	250		11.00	2.00
2017	12.21	11.63	-0.58	248		11.00	2.00
2018	12.36	11.65	-0.69	245		11.00	2.00
2019	12.50	11.88	-0.62	241		11.00	2.00
2020	12.65	11.90	-0.75	238	0.20	11.20	2.00
2021	12.83	11.93	-0.90	231		11.20	2.00
2022	12.97	11.95	-1.02	228		11.20	2.00
2023	13.12	11.97	-1.15	220		11.20	2.00
2024	13.27	12.00	-1.27	213		11.20	2.00
2025	13.39	12.02	-1.37	206		11.20	2.00
2026	13.49	12.04	-1.45	199		11.20	2.00
2027	13.59	12.06	-1.52	191		11.20	2.00
2028	13.65	12.08	-1.57	182		11.20	2.00
2029	13.69	12.10	-1.58	174		11.20	2.00
2030	13.70	12.12	-1.58	166		11.20	2.00
2031	13.69	12.14	-1.55	157		11.20	2.00
2032	13.67	12.15	-1.52	149		11.20	2.00
2033	13.64	12.17	-1.47	141		11.20	2.00
2034	13.57	12.18	-1.39	134		11.20	2.00
2035	13.48	12.19	-1.29	127		11.20	2.00
2036	13.37	12.19	-1.17	121		11.20	2.00
2037	13.25	12.20	-1.05	116		11.20	2.00
2038	13.12	12.21	-0.91	111		11.20	2.00
2039	12.98	12.21	-0.77	107		11.20	2.00
2040	12.84	12.42	-0.42	105	0.20	11.40	2.00
2041	12.70	12.42	-0.27	104		11.40	2.00
2042	12.57	12.42	-0.14	105		11.40	2.00
2043	12.45	12.43	-0.02	107		11.40	2.00
2044	12.35	12.43	0.09	110		11.40	2.00
2045	12.25	12.44	0.19	114		11.40	2.00
2046	12.15	12.44	0.29	118		11.40	2.00
2047	12.07	12.45	0.38	124		11.40	2.00
2048	11.99	12.46	0.46	130		11.40	2.00
2049	11.93	12.46	0.54	137		11.40	2.00
2050	11.87	12.47	0.60	145		11.40	2.00
2051	11.82	12.48	0.65	154		11.40	2.00
2052	11.79	12.48	0.69	163		11.40	2.00
2053	11.77	12.49	0.73	172		11.40	2.00
2054	1R.75	12.50	0.75	182		11.40	2.00
2055	11.73	12.51	0.77	192		11.40	2.00
2056	11.73	12.52	0.79	203		11.40	2.00
2057	11.72	12.53	0.81	214		11.40	2.00
2058	11.72	12.54	0.82	225		11.40	2.00
2059	11.71	12.54	0.83	237		11.40	2.00
2060	11.71	12.75	1.04	249	0.20	11.60	2.00
2061	11.70	12.76	1.06	263		11.60	2.00
2062	11.68	12.77	1.09	277		11.60	2.00
2063	11.65	12.77	1.12	293		11.60	2.00
2064	11.62	12.78	1.16	309		11.60	2.00
2065	11.59	12.78	1.19	325		11.60	2.00
2066	11.57	12.79	1.22	343		11.60	2.00
2067	11.56	12.79	1.25	361		11.60	2.00
2068	11.51	12.80	1.28	380		11.60	2.00
2069	11.49	12.80	1.31	400		11.60	2.00
2070	11.46	12.80	1.34	420		11.60	2.00
2071	11.44	12.81	1.37	441		11.60	2.00
2072	11.43	12.81	1.38	463		11.60	2.00
2073	11.41	12.81	1.40	485		11.60	2.00
2074	11.43	12.82	1.39	505		11.60	2.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	12.19	12.48	0.28	2.35

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback

Office of the Actuary
Social Security Administration
June 3, 1999

SOCIAL SECURITY ADMINISTRATION
May 25, 1999

Harry C. Ballantyne, Chief Actuary

Memorandum

Refer To: TCC

Subject: Estimated Long-Range OASDI Financial Effects of the 21st Century Retirement Security Act

This memorandum provides long-range estimates of the financial status of the OASDI program of the 21st Century Retirement Security Act (H.R. 1793), proposed by Representatives Kolbe and Stenholm. The principal staff contacts are Ed Lorenzen and Joan Hay from Representative Stenholm's staff. All estimates are based on the intermediate assumptions of the 1999 Trustees Report. This memorandum supersedes the memorandum dated May 12, 1999, and reflects minor modifications made after May 12 in the specification of provisions 7 and 9.

The provisions described in this memorandum reflect the intent of legislation as described by Representative Stenholm's staff. The stated intent of several provisions differs from the legislative language in the bill. These discrepancies are indicated in the attached table, and are described in the provision descriptions below. Discrepancies are indicated for provisions 1, 2, 6, and 7a. Representative Stenholm's staff indicates that technical amendments to the bill to conform with the stated intent will be forthcoming.

The comprehensive proposal detailed in the 21st Century Retirement Security Act reduces OASDI benefits from the levels provided under present law so that the program can be adequately financed with a combined payroll tax rate of 10.4 percent. The other 2.0 percentage points of the 12.4 percent combined Social Security payroll tax rate is redirected to mandatory individual accounts, collected, held and managed by the Federal Government. Individuals will have a choice of different investment options for their individual accounts, which includes a stock index fund, a bond index fund, and a Treasury securities index fund. The changes to the OASDI program are designed to achieve long-range actuarial balance, and to result in a combined OASDI trust fund ratio (ratio of trust fund assets to annual outgo) that is stable or rising at the end of the long-range 75-year period.

The proposal would improve the long-range OASDI actuarial balance by an estimated 2.14 percent of taxable payroll, replacing the present-law actuarial deficit of 2.07 percent with an actuarial balance of +0.07 percent of taxable payroll. The OASDI annual balance for the year 2070 would improve by 6.63 percent of payroll, to a level of +0.34 percent of payroll. The trust fund ratio for the combined OASDI program would increase to a peak of 244 percent in 2010, then decline to 8 percent in 2044. After 2044, the trust fund ratio would begin to rise, reaching 194 percent at the end of the long-range period, at which time the ratio would be rising by about 6 percentage points per year.

Table 1 provides a brief listing of the individual provisions of the proposal, including the effect of each provision, separately, on the long-range OASDI actuarial balance. A more detailed description of the provisions for which these estimates have been developed is given below.

PROVISION 1: REDUCE THE COLA BY 0.33 PERCENTAGE POINT

This provision is intended to reduce the present-law OASDI cost-of-living adjustment (COLA) for monthly OASDI benefits by 0.33 percentage point from the level currently anticipated under the assumptions of the 1999 Trustees Report. The reduction would start with the COLA scheduled for December 2000 and continue indefinitely thereafter. Specifically, the provision would provide for two reductions in the COLA. First, the COLA would be reduced by the amount of upper-level substitution bias that would be alleviated by using a superlative formula, as estimated by the Bureau of Labor Statistics (BLS). This bias is generally assumed to be an average of 0.15 percentage point per year. Second, the COLA would be reduced by 0.33 percentage point less the sum of (a) the estimated upper-level substitution bias described above and (b) the achieved substitution bias correction, i.e., the estimated net effect of changes to the CPI-W instituted by the BLS after January 31, 1999.

A technical amendment to H.R. 1793 is anticipated to clarify this provision. The definition currently in the bill for achieved substitution bias correction would in-

clude changes instituted after December 31, 1998, thus including the geometric means provision instituted in January 1999 to address lower-level substitution bias in the CPI-W. Because the geometric means change was intended to be excluded from the definition of achieved substitution bias correction, the technical amendment will change the definition to include changes instituted after January 31, 1999.

Provision 2: Increase NRA and EEA; Modify Actuarial Reduction and Increment Factors

Increase NRA and EEA

Increase the normal retirement age (NRA) and the earliest eligibility age (EEA) allowed for retired worker and aged spouse benefits. NRA increases under current law from 65 by two months a year beginning with individuals attaining age 62 in the year 2000, until it reaches 66 for individuals attaining age 62 in the year 2005. While current law then leaves the NRA at 66 for several years, this provision would continue to phase the NRA upwards by two months a year until it reaches 67 for individuals reaching age 62 in 2011. After 2011, the NRA would increase by one month every two years. Based on current mortality projections, this scheduled increase would maintain the ratio of expected retirement years at NRA to potential work years (from age 20 to NRA) constant at the level for 2011.

This provision would also increase the earliest eligibility age (EEA) for retired worker and aged spouse benefits after 2011 at the same rate by which the NRA is increase after 2011. This would maintain the five-year differential between NRA and EEA that is achieved for those eligible for benefits in 2011, when the NRA is 67 and the EEA is still 62. It should be noted that the description of the increase in EEA currently in H.R. 1793 would not achieve the intended result described above. A technical amendment to H.R. 1793 that will eliminate this discrepancy is anticipated.

The NRA and EEA, for individuals turning age 62 in 2035, would be 68 and 63, respectively.

The earliest eligibility age for receiving aged widow/widower's benefits remains unchanged at 60. For disabled widow/widowers, the earliest eligibility age is also retained, at 50.

Each time the EEA is increased by a full year, the number of elapsed years for retired workers is also extended one year. This would result in an increase in the benefit computation period of one year.

Furthermore, the age up to which earnings are indexed in computing the AIME for the PIA benefit formula would be increased by one year. Because the applicable PIA formula is the formula in effect for the year of initial benefit eligibility, the PIA formula would also be advanced one year.

Modify Actuarial Reduction and Increment Factors

In addition, the early retirement factors and delayed retirement credits would be changed in an attempt to reflect the fact that the marginal increase in the full (PIA) benefit level for earnings after reaching retirement age is, generally, relatively small. (Reduction and increment factors provided under current law are intended to provide actuarially equivalent lifetime benefits payable at different starting ages for a fixed earnings history.) This relatively small marginal increase results from the weighted PIA benefit formula, which provides a larger marginal amount of benefit per dollar of AIME for low, or early-in-career, earnings. This provision is intended to eliminate the marginal disincentive to work past EEA that is provided by the weighting in the PIA formula. Because the extent of this marginal effect depends upon the level of earnings a worker has had in earlier years, no absolute adjustment can be provided that would be appropriate for all workers. Rough estimates of adjustments to the reduction and increment factors have thus been used.

The chart below displays the proposed monthly early retirement reductions that are applicable for retired worker beneficiaries for the first 36 months for which benefits are received prior to NRA under both current law and the provision. (Different factors apply to aged spouse beneficiaries and aged widow beneficiaries.)

Monthly Reduction in Benefits for Each of First 36 Months of Retirement Before NRA

Age 62 in:	2001	2002	2003	2004	2005	2006+
Present Law	20/36%	20/36%	20/36%	20/36%	20/36%	20/36%
Proposal	20/36%	21/36%	22/36%	23/36%	24/36%	25/36%

Similar increases for aged spouse beneficiaries would be applied, increasing the monthly reduction for the first 36 months of entitlement before NRA from 25/36 percent under present law to 30/36 percent under the provision.

The reductions that are proposed for the fourth and fifth year before NRA are 12/24% per month (current law reductions are 10/24% per month) for both retired worker and aged spouse beneficiaries. The reductions for the fourth and fifth year before NRA are applicable to all new eligibles who reach age 62 after 1999.

The delayed retirement credit (DRC) under present law is scheduled to increase to 8% per year for workers attaining age 65 after 2007. The DRC would continue to increase at the rate of 0.5 percentage point every two years, with the first increase applied to those attaining age 65 in 2010. An ultimate factor of 10 percentage points per year is reached for workers reaching 65 after 2015. The delayed retirement credit applies for months for which retired worker benefits are not received between NRA and age 70.

The ultimate percentages of PIA payable for retired workers by age at initial benefit entitlement are shown in the table below.

Ultimate Percent of PIA Payable for Retired Worker Beneficiaries by Age at Initial Entitlement to Benefits

Age at Initial Entitlement:	NRA–5	NRA–4	NRA–3	NRA–2	NRA–1	NRA
Present Law	70%	75%	80%	86.7%	93.3%	100%
Proposal	63%	69%	75%	83.3%	91.7%	100%

The percentage of PIA payable for non-disabled aged widow beneficiaries newly eligible at age 60 would remain at 71.5 percent. The percentages payable for those newly eligible at ages between 60 and the NRA would scale linearly between 71.5 and 100 percent, as under present law.

Provision 3: Change in calculation of AIME

This provision would apply in determining benefits for retired worker and their dependents and for survivors of deceased workers. This provision does not apply in determining benefits for disabled workers and their dependents.

In calculating the AIME for a retired worker under present law, the highest 35 years of indexed earnings are used in determining the numerator of the AIME and a benefit computation period of 35 years is used in determining the denominator. Under this provision, the following changes are made in the calculation of the AIME for someone newly eligible for retirement benefits after 2001.

- The number of years of earnings, used in calculating the numerator of the AIME, is gradually increased, reaching all years of earnings in 2010.
- The benefit computation period, used in determining the denominator of the AIME, is gradually increased, reaching 40 years (5 additional years), except for the lower earner of a married couple. In the case of a two-earner couple, the benefit computation period for the earner with the lower PIA is 35 years.

The chart below indicates the phase in schedule of the above changes.

Change in Calculation of AIME for Retired Worker

(assumes the retired worker is not the lower earner of a married couple)

Newly Eligible in Years:	2002–2003	2004–2005	2006–2007	2008–2009	2010+
Present Law					
Years in Numerator [1]	35	35	35	35	35
Denominator (in years) [2]	35	35	35	35	35
Proposal					
Years in Numerator [1]	37	39	41	43	all
Denominator (in years) [2]	36	37	38	39	40

[1] Years in Numerator: Refers to the number of years of earnings used in calculating the numerator of the AIME.

[2] Denominator (in years): Refers to the benefit computation period (in years) used in calculating the denominator of the AIME.

Under this provision alone, the number of benefit computation years used for the denominator of the AIME for a retired worker turning age 62 after 2009 would be 40. Under current law, the number of benefit computation years is determined by subtracting 5 dropout years from the number of elasped years (years age 22 through the year prior to reaching EEA). Under this proposed provision, the increase in the number of benefit computation years would be accomplished by reducing the number of dropout years, ultimately to zero. In addition, each year, except for 2010, that the number of dropout years is reduced by one year, the number of years of earnings, used in calculating the numerator of the AIME, is increased an additional two years. In 2010, all years of earnings are used in calculating the numerator of the AIME for someone newly eligible for retirement or survivor benefits.

Provision 4: Eliminate the Earnings Test at the Normal Retirement Age (NRA)

Effective 1/1/2000, this provision would eliminate the earnings test at NRA, which requires a reduction in the monthly benefit payable to individuals at or above NRA by $1 for every $3 that their earnings exceed a specified exempt amount. The long-range cost of this provision is negligible because months for which benefits are withheld result in later recomputation of the percent of PIA payable. Thus, the earnings test does not reduce expected lifetime benefits, but defers benefits until substantial earnings have ceased.

Provision 5: Credit All Revenue from Taxation of OASDI Benefits to OASDI by 2019

This provision redirects revenue collected by the IRS from Federal income taxes payable on OASDI benefits, in excess of the tax on 50 percent of such benefits, from the Medicare HI trust fund to the OASDI trust funds. The provision would redirect 10 percent of this revenue for 2010, 20 percent for 2011, ... , and 100 percent for 2019 and later.

Provision 6: Establish a minimum PIA level

For beneficiaries newly eligible in 2010 and later, establish a minimum PIA amount as described below:

For Retired Workers:

The minimum PIA would apply to retired workers with at least 80 quarters of coverage. It would equal 60% of the Monthly Applicable Poverty Level (see below for definition) for individuals with 80 quarters of coverage and 100% of the Monthly Applicable Poverty Level for individuals with at least 160 quarters of coverage. The percentage of the Monthly Applicable Poverty Level defining the minimum PIA for an individual with more than 80 quarters and less than 160 quarters of coverage would be prorated between 60% and 100%, based on their number of quarters of coverage.

For Disabled Workers:

A minimum PIA for disability beneficiaries would be similar, equaling 60% of the Monthly Applicable Poverty Level for individuals whose quarters of coverage equal to twice the number of their elasped years (years between attaining age 22 disability benefit entitlement) and 100% of the Monthly Applicable Poverty Level for

individuals whose quarters of coverage equal four times their number of elasped years.

The minimum PIA is phased in during the years 2006 through 2009. For new eligibles in 2006, the percentage of the Monthly Applicable Poverty Level is one-fifth of the fully phased in percentage in 2010. This fraction increases by one-fifth for each year during the phase in period, reaching four-fifths for 2009.

The Annual Applicable Poverty Level for 1998 is $7,818 (Monthly Applicable Poverty Level would equal 1/12 of this amount). It should be noted that the current bill language of H.R. 1793 would establish this level as $7,992 for 1996. A technical amendment to H.R. 1793 that will eliminate this discrepancy is anticipated. The Annual Applicable Poverty Level that applies to an individual in their year of initial eligibility is determined by increasing the 1998 level by:

1. the COLA for 1998 through the earlier of (1) the year prior to the year of initial benefit eligibility and (2) 2009; and

2. increases in the average wage index between 2008 and the second year prior to initial benefit eligibility.

Minimum PIA levels would increase by the COLA after benefit eligibility in all cases.

Provision 7: Modification of PIA Formula

Provision 7a reduces the primary insurance amount (PIA) of those who become eligible for benefits after 2011 by multiplying the PIA successively by a factor of 0.995. The number of times the PIA is multiplied by the factor of 0.995 is equal to the number of years beginning with 2012 through the earlier of the year in which the beneficiary reaches initial benefit eligibility (or death) and 2044. A technical amendment to H.R. 1793 is anticipated to clarify that 2044 is the last year for which the factor of 0.995 would apply to the PIA (the current bill indicates that 2045 is the last year). The ultimate reduction in the PIA level for beneficiaries newly eligible in 2044 and later would be 15.2 percent.

Provision 7b reduces the upper two factors of the PIA benefit formula (32 and 15) by 1.5 percent per year (multiply by 0.985) for 2006 through 2010 and by 2 percent per year (multiply by 0.98) for 2011 through 2030. The upper two PIA benefit factors applicable for beneficiaries newly eligible in 2030 and later would be 19.8 and 9.3 percent, respectively.

Provision 8: Redirect 2 Percentage Points of Payroll Tax

This provision would redirect 2 percentage points of the employee's share of the FICA payroll tax for the funding of an individual savings account, for OASDI taxable earnings after 1999 of workers who were under age 55 at the beginning of the year 2000. A similar redirection would occur for taxable self-employment earnings, with 2 percentage points of taxable self-employment income redirected to individual accounts. All earnings would be collected by the Federal Government in the same manner that payroll taxes are collected currently. Accounts would be managed and invested, under the direction of the worker, centrally, as suggested by the Advisory Council Individual Account proposal.

Provision 9: Transfer money from General Revenue to the OASI Trust Fund

This provision provides a transfer to the OASI Trust Fund from the General Fund of the Treasury. The amounts to be transferred are specified as an increasing percentage of OASDI taxable payroll and are as follows:

Calendar Year	Percent of Taxable Payroll	Calendar Year	Percent of Taxable Payroll	Calendar Year	Percent of Taxable Payroll
2000	0.03	2005	0.24	2010–2015	0.47
2001	0.07	2006	0.28	2016–2039	0.55
2002	0.13	2007	0.32	2040–2059	0.66
2003	0.15	2008	.035	2060+	0.80
2004	0.20	2009	.038		

Stephen C. Goss
Deputy Chief Actuary
Alice H. Wade
Actuary

Attachment

Table 1. Estimated Long-Range OASDI Financial Effect of the 21st Century Retirement Security Act (Kolbe/Stenholm)

	Provision	Estimated Change in Long-range OASDI Actuarial Balance (percent of taxable payroll)
1	Reduce the COLA for OASDI benefits by 0.33 percentage point beginning Dec. 2000.	0.50
2	Eliminate the hiatus in the currently scheduled increase in NRA and increase the NRA beyond 67 by indexing to maintain the ratio of expected retirement years to expected work years constant (one month increase every two years under current mortality assumptions). In addition, increase the EEA to maintain a five-year differential between NRA and EEA. Increase early retirement factors and delayed retirement credits (to reflect marginal gain in benefit for work after retirement age).	0.80
3	Increase the benefit computation period by up to 5 additional years for new eligibles (by one additional year for new eligibles in each year 2002, 2004, 2006, 2008, 2010). For two-earner couples, however, cap the benefit computation period for the earner with the lower PIA at 35 years. In conjunction with increasing the benefit period, phase in including earnings for all years in calculating the AIME. This provision does not apply to disabled worker beneficiaries.	0.19
4	Effective 1/1/2000, eliminate the retirement earnings test for individuals who are at or past NRA.	[1]
5	Credit all revenue from taxation of OASDI benefits to the OASDI trust funds by 2019 (phase revenue from HI to OASDI during the period 2010–2019).	0.30
6	Beginning in 2006, establish a minimum PIA level for newly eligible beneficiaries with quarters of coverage equal to twice their number of elasped years. The minimum PIA level will be fully phased in 2010, equaling 100% of the applicable poverty level for newly eligible beneficiaries with quarters of coverage equal to four times their number of elasped years (60% of the applicable poverty level for beneficiaries with quarters of coverage equal to twice elapsed years).	−0.15
7a	Reduce PIA levels by 0.5 percent (multiply by 0.995) for each year 2012–2044.	0.83
7b	Reduce the 32 and 15 PIA-formula factors by 1.5 percent for each year 2006–2010 and by 2 percent for each year 2011–2030. Factors for 2030 are 19.8 and 9.3, respectively (not interacted with 7a).	1.66
8	For workers under age 55 in 2000, redirect 2 percentage points of the OASDI payroll tax to individual accounts.	−1.90
9	Transfer amounts (specified as percentages of taxable payroll) to the OASI Trust Fund from the General Fund of the Treasury.	0.50
	Total for Provisions 1 through 9 (including interaction among provisions)	2.14

[1] Negligible (between −0.005 and .005 percent of payroll) change in the OASDI long-range actuarial balance.
[2] Technical amendments to H.R. 1793 that reflect this description are to follow, see text for details.

Based on the intermediate assumptions of the 1999 Trustees Report under present law, the long-range actuarial balance for the 75-year period (1999–2073) is −2.07 percent of taxable payroll.

May 25, 1999 Office of the Chief Actuary Social Security Administration

SOCIAL SECURITY ADMINISTRATION
June 8, 1999

Harry C. Ballantyne, Chief Actuary

Memorandum

Refer To: TCC

Subject: Estimates of Long-Range OASDI Financial Effect of Proposal for Representative Peter DeFazio—INFORMATION

This memorandum provides long-range estimates of the effect on the financial status of the OASDI program of a proposed plan to change several provisions of the program. This analysis has been produced at the request of Aaron Deas of Representative DeFazio's staff. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

The comprehensive proposal is described in Table A, attached. Table Aprovides estimates of the change in the long-range OASDI actuarial balance that would result from the enactment of the total proposed package, as well as from each individual provision of the proposed package.

If all modifications are implemented, the resulting long-range actuarial balance for the 75-year period (1999–2073) is estimated to be +0.07 percent of taxable payroll. This is a change of +2.14 from the long-range actuarial balance under present law of −2.07 percent of taxable payroll. The combined OASDI Trust Fund would rise to a peak of 579 percent of annual cost for 2021, declining thereafter, and reaching a level of 217 percent of annual cost at the end of the long-range period.

STEPHEN C. GOSS
Deputy Chief Actuary
ALICE H. WADE
Actuary

Table A. Estimated Long-Range OASDI Financial Effect of Reform Proposal (Rep. DeFazio)

	Provision	Estimated Change in Long-range OASDI Actuarial Balance (percent of taxable payroll
1	Invest a portion of the OASDI Trust Funds in stocks beginning in 2000, reaching 40 percent of assets in stocks for 2014 and later.	1.01
2	For earnings in years after 1999, change the OASDI contribution and benefit base to be a benefit base only. Subject all covered earnings to OASDI payroll taxes, but use the base to establish the maximum annual amount of earnings that is credited for the purpose of benefit computation.	2.02
3	Beginning in 2000, establish an exempt amount for a worker's annual taxable earnings. The exempt amount would be set at $4,000 in 2000, and would serve to exempt the first $4,000 of each worker's annual taxable earnings from the 6.2 percent employee's tax. For self-employed individuals, the provision would exempt the first $4,000 of self-employment income from one half of the 12.4 percent self-employed tax rate. The $4,000 would be included in determining benefit amounts. For years after 2000, the exempt amount would be indexed by growth in the SSA average wage index.	−1.03
4	In 2020, increase the level of benefits for all beneficiaries who are age 85 or older by 5 percent. This increase is phased in beginning in 2001. Benefit payments for beneficiaries meeting this age requirement would increase by 0.25 percent for 2001, 0.5 percent for 2002, etc., reaching 0.5 percent for 2020 and later.	−0.05
5a	Increase the benefit computation period by up to 5 additional years for new eligibles (by one additional year for new eligibles in each year 2005, 2007, 2009, 2011, 2013).	0.35

Table A. Estimated Long-Range OASDI Financial Effect of Reform Proposal (Rep. DeFazio)—Continued

	Provision	Estimated Change in Long-range OASDI Actuarial Balance (percent of taxable payroll
5b	Provide up to 5 child-care drop-out years. These years will be granted to a parent who has $0 earnings during the year and is providing care to his/her child under the age of 12 or to his/her disabled child. Drop-out years are phased in by one additional year for new eligibles in each year 2005, 2007, 2009, 2011, 2013. (This provision reflects interaction with provision 5a.)	–0.15
	Total for Provisions 1 through 5 (including interaction among provisions)	2.14

Based on the intermediate assumptions of the 1999 Trustees Report under present law, the long-range actuarial balance for the 75-year period (1999–2073) is −2.07 percent of taxable payroll.
June 8, 1999 Social Security Administration Office of the Chief Actuary

SOCIAL SECURITY ADMINISTRATION
June 3, 1999

Harry C. Ballantyne, Chief Actuary

Memorandum

Refer To: TCC

Subject: Long-Range OASDI Financial Effects of a Proposal for Representative Nadler—INFORMATION

This memorandum updates estimates provided for this proposal on February 25, 1999, based on the intermediate assumptions of the 1998 Trustees Report and the ultimate yield on stock assumed for the President's plan under 1998 Trustees assumptions. Updated estimates reflect the intermediate assumptions of the 1999 Trustees Report and the ultimate real yield on stock assumed by the 1994–96 Advisory Council on Social security.

This proposal would eliminate the long-range OASDI actuarial deficit estimated under the intermediate assumptions of the 1999 Trustees Report by enacting two provisions. First, the OASDI benefit and contribution base would be increased to $99,600 for the year 2000, $117,900 for 2001, with increases thereafter sufficient to have 90 percent of estimated OASDI covered earnings subject to the payroll tax. This provision alone would reduce the long-range OASDI actuarial deficit by an estimated 0.61 percent of taxable payroll.

The second provision would call for transfers to be made from the General Fund of the Treasury of the United States to the Old-Age, Survivors, and Disability Insurance (OASDI) trust funds for each year 2000 through 2014. The amount of transfer for each year would be specified in law as a percentage of the OASDI effective taxable payroll. In each year 2000 through 2014, 40 percent of the transfer would be used to purchase stock and 60 percent would be used to purchase special interest-bearing obligations of the Treasury. All dividends would be reinvested in stock until the market value of all stock held by the OASDI trust funds reached 30 percent of total OASDI trust fund assets. Thereafter, the percentage of total trust fund assets that is held in stocks would be maintained at 30 percent. This provision would reduce the OASDI actuarial deficit by an additional 1.94 percent of payroll.

Enactment of these two provisions would result in benefits being payable throughout the long-range period under the intermediate assumptions of the 1999 Trustees Report. Trust fund assets as a percentage of OASDI outgo (the trust fund ratio) would rise, reaching a peak of 923 percent for the year 2017. The trust fund ratio would generally decline thereafter, reaching 793 percent at the end of the long-range period (at the end of 2073), at which point the trust fund ratio would be estimated to be declining at about 7 percentage points per year. These provisions would improve the long-range OASDI actuarial balance by an estimated 2.55 percent of payroll, replacing the actuarial deficit of 2.07 percent under present law with an es-

timated positive actuarial balance of 0.48 percent of payroll. These estimates are based on the intermediate assumptions of the 1999 Trustees Report and other assumptions described below.

Transfers from the General Fund of the Treasury would be made each year 2000 through 2014 in amounts equal to the then-current estimates of OASDI effective taxable payroll, multiplied by the percentages in the table below. Revisions in amounts transferred each year would be made as estimates of taxable payroll for the year are finalized.

Amount To Be Transferred to the OASDI Trust Funds: Specified Percentage of OASDI Effective Taxable Payroll

2000	2.20%	2005	2.55%	2010	4.32%
2001	1.75%	2006	3.07%	2011	4.49%
2002	2.20%	2007	3.43%	2012	4.58%
2003	2.08%	2008	3.79%	2013	4.61%
2004	2.41%	2009	4.12%	2014	4.51%

The percentages of payroll to be transferred are consistent with the amounts that would have been transferred under the President's plan (announced in the January 19, 1999 State of the Union speech) using the intermediate estimates of the 1998 Trustees Report, as shown in our memorandum dated February 12, 1999.

Actual transfers for each year would be specified as the product of (a) the specified percentage of OASDI effective taxable payroll (indicated above, consistent with the President's plan), and (b) the then-current estimated taxable payroll at the beginning of each year of transfer. As estimates of taxable payroll for each year are revised with increasingly complete data, adjustments to transfers for the year would be made.

Table 1, attached, provides annual estimates of the OASDI income rate, cost rate, annual balance and trust fund ratio.

OASDI Trust Fund Assets in Stock

Estimates for this proposal are based on an assumption that the average ultimate total annual real yield on stock will average 7 percent in the future, consistent with the assumption used for the 1994–6 Advisory Council on Social Security. The four-percentage-point difference between this assumed ultimate real stock yield and the Trustees' 3-percent assumed ultimate real yield on government bonds held by the trust funds is assumed to be maintained throughout the 75-year projection period.

The percentage of the OASDI combined trust funds that is held in stock is estimated to reach 30 percent in the year 2021. If the average yield on stocks is greater or less than assumed over the period 2000–21, the year in which the specified level of 30 percent of assets in stock is reached would be sooner or later than 2021.

The portion of the total value of publicly-traded stock in the United States that is held by the OASDI trust funds will depend not only on the yield achieved in the market, but also on the rate of growth in the total market value of all stock. The total value of stock represented in the Wilshire 5000 index (a fair representation of all publicly-traded stock for corporations based in the United States) was $9.3 trillion at the beginning of 1998. Assuming that the total market value of publicly-traded stock will rise generally by the rate of growth in GDP after 1998, the trust funds would hold about 12.5 percent of the total market value, on average, over the next 50 years.

Average Percentage of Total Stock Market Value Held by OASDI

2001–14	3.9%
2001–20	6.4%
2001–30	9.6%
2001–40	11.4%
2001–50	12.5%

Stephen C. Goss
Deputy Chief Actuary
Alice H. Wade
Actuary

Attachment

Table 1. Rep Nadler Proposal: OASDI Annual Rates and Trust Fund Ratios

Calendar Year	Income Rate	Cost Rate	Annual Balance	TFR
1999	12.70	10.80	1.90	194
2000	14.84	10.40	4.44	217
2001	14.41	10.29	4.12	263
2002	14.86	10.35	4.51	306
2003	14.75	10.41	4.34	352
2004	15.08	10.47	4.61	396
2005	15.23	10.55	4.68	440
2006	15.76	10.64	5.12	486
2007	16.13	10.74	5.38	533
2008	16.50	10.86	5.64	583
2009	16.84	11.03	5.81	633
2010	17.06	11.21	5.85	685
2011	17.23	11.42	5.81	736
2012	17.33	11.66	5.67	785
2013	17.37	11.93	5.44	833
2014	17.29	12.22	5.07	878
2015	12.79	12.52	0.27	919
2016	12.81	12.85	-0.04	922
2017	12.83	13.19	-0.36	922
2018	12.85	13.53	-0.68	922
2019	12.87	13.89	-1.02	919
2020	12.89	14.24	-1.36	915
2021	12.91	14.59	-1.68	912
2022	12.93	14.90	-1.98	908
2023	12.94	15.22	-2.28	904
2024	12.96	15.52	-2.56	900
2025	12.98	15.81	-2.83	895
2026	13.00	16.08	-3.08	891
2027	13.01	16.33	-3.31	886
2028	13.03	16.55	-3.52	882
2029	13.05	16.74	-3.69	877
2030	13.06	16.91	-3.85	874
2031	13.07	17.06	-3.98	870
2032	13.09	17.19	-4.10	867
2033	13.10	17.30	-4.20	864
2034	13.11	17.38	-4.27	862
2035	13.11	17.42	-4.31	862
2036	13.12	17.45	-4.33	862
2037	13.13	17.47	-4.34	862
2038	13.13	17.47	-4.34	863
2039	13.14	17.47	-4.33	865
2040	13.14	17.46	-4.32	867
2041	13.15	17.46	-4.31	869
2042	13.15	17.46	-4.31	871
2043	13.16	17.47	-4.31	874
2044	13.16	17.48	-4.32	876
2045	13.16	17.49	-4.33	878
2046	13.17	17.51	-4.34	880
2047	13.17	17.54	-4.37	881
2048	13.18	17.57	-4.39	883
2049	13.18	17.61	-4.43	884
2050	13.19	17.66	-4.47	884
2051	13.20	17.72	-4.52	885
2052	13.20	17.79	-4.59	884
2053	13.21	17.87	-4.66	883
2054	13.22	17.95	-4.74	881
2055	13.22	18.04	-4.82	879
2056	13.23	18.13	-4.89	876
2057	13.24	18.21	-4.97	873
2058	13.25	18.29	-5.05	870
2059	13.25	18.37	-5.12	867
2060	13.26	18.45	-5.19	863
2061	13.27	18.52	-5.25	860
2062	13.27	18.58	-5.31	856
2063	13.28	18.65	-5.37	852
2064	13.28	18.71	-5.42	848
2065	13.29	18.76	-5.48	843
2066	13.29	18.82	-5.53	839
2067	13.30	18.87	-5.57	834
2068	13.30	18.92	-5.62	829
2069	13.31	18.97	-5.66	824
2070	13.31	19.02	-5.71	818
2071	13.32	19.07	-5.76	813
2072	13.32	19.12	-5.80	806
2073	13.32	19.18	-5.85	800
2074	13.33	19.23	-5.90	793
2075	13.33	19.28	-5.95	786

Based on the intermediate assumptions of the 1999 Trustees Report and 7% real stock yield.
Office of the Chief Actuary
Social Security Administration

3-Jun-99

SOCIAL SECURITY ADMINISTRATION
June 8, 1999

Harry C. Ballantyne, Chief Actuary

Memorandum

Refer To: TCC

Subject: Estimated Long-Range OASDI Financial Effect of Proposal by Representative Mark Sanford—INFORMATION

This memorandum provides the estimated effect on long-range OASDI financial status of a proposal developed for Representative Mark Sanford. Specifications for this proposal have been provided by Joel Mowbray and Scott English of Representative Sanford's staff.

This proposal would:

(1) modify OASDI benefits,

(2) provide transfers from the Treasury to the DI trust fund, to maintain benefit payments,

(3) make contributions from the U.S. Treasury (from the OASI trust fund in part after 2043) equal to the amount of any excess of OASI income over cost, each year (up to 5 percent of taxable earnings), to workers for investment in Individual Accounts (IAs), and

(4) reduce each worker's OASI benefits, by an amount equal to the value of IA contributions accumulated at the yield on OASI trust fund assets. Include all proceeds of the IAs with OASDI benefits for income taxation, with the revenue transferred to the OASI and HI trust funds as under present law.

The balance of this memorandum provides a description of the proposal and estimates of the long-range financial effects of the proposal on the OASDI program. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

SUMMARY OF PROPOSAL PROVISIONS

(1a) Raise the normal retirement age (NRA) at the rate of
2 months per year beginning in the year 2000, until reaching an NRA of 67 for persons attaining age 62 in 2011 (eliminate the hiatus in current law).

(1b) Change the early retirement factors and delayed retirement credits in an attempt to reflect the fact that the marginal increase in the full (PIA) benefit level for earnings after reaching retirement age is, generally, relatively small. (Reduction and increment factors provided under current law are intended to provide actuarially equivalent lifetime benefits payable at different starting ages for a fixed earnings history.) This relatively small marginal increase results from the weighted PIA benefit formula, which provides a larger marginal amount of benefit per dollar of AIME for low, or early-in-career, earnings. This provision is intended to eliminate the marginal disincentive to work past EEA that is provided by the weighting in the PIA formula. Because the extent of this marginal effect depends upon the level of earnings a worker has had in earlier years, no absolute adjustment can be provided that would be appropriate for all workers. Rough estimates of adjustments to the reduction and increment factors have thus been used.

The chart below displays the proposed monthly early retirement reductions that are applicable for retired worker beneficiaries for the first 36 months for which benefits are received prior to NRA under both current law and the provision. (Different factors apply to aged spouse beneficiaries and aged widow beneficiaries.)

Monthly Reduction in Benefits for Each of First 36 Months of Retirement Before NRA

Age 62 in:	2009	2010	2011	2012	2013	2014+
Present Law	20/36%	20/36%	20/36%	20/36%	20/36%	20/36%
Proposal	20/36%	21/36%	22/36%	23/36%	24/36%	25/36%

Similar increases for aged spouse beneficiaries would be applied, increasing the monthly reduction for the first 36 months of entitlement before NRA from 25/36 percent under present law to 30/36 percent under the provision.

The reductions that are proposed for the fourth and fifth year before NRA are 12/24% per month (current law reductions are 10/24% per month) for both retired

worker and aged spouse beneficiaries. The reductions for the fourth and fifth year before NRA are applicable to all new eligibles who reach age 62 after 1999.

The ultimate percentages of PIA payable for retired workers by age at initial benefit entitlement are shown in the table below.

Ultimate Percent of PIA Payable for Retired Worker Beneficiaries by Age at Initial Entitlement to Benefits

Age at Initial Entitlement:	NRA–5	NRA–4	NRA–3	NRA–2	NRA–1	NRA
Present Law	70%	75%	80%	86.7%	93.3%	100%
Proposal	63%	69%	75%	83.3%	91.7%	100%

The delayed retirement credit (DRC) under present law is scheduled to increase to 8% per year for workers attaining age 65 after 2007. The DRC would continue to increase at the rate of 0.5 percentage point every two years, with the first increase applied to those attaining age 65 in 2010. An ultimate factor of 10 percentage points per year is reached for workers reaching 65 after 2015. The delayed retirement credit applies for months for which retired worker benefits are not received between NRA and age 70.

The percentage of PIA payable for non-disabled aged widow beneficiaries newly eligible at age 60 would remain at 71.5 percent. The percentages payable for those newly eligible at ages between 60 and the NRA would scale linearly between 71.5 and 100 percent, as under present law.

(1c) For years 2009 through 2028, reduce the 15-percent PIA factor by 2 percent per year (multiply by 0.98 each year). For years 2028 and later, the factor would be 10 percent.

(1d) Effective 2001, eliminate the retirement earnings test applicable to earnings of beneficiaries who have reached the normal retirement age (NRA).

(2) Transfer from the General Fund of the Treasury to the Disability Insurance (DI) trust fund, each year, any amount needed to permit full payment of DI benefits.

(3) Make contributions from the General Fund of the Treasury each year starting with 2001, to individual accounts of workers with OASDI taxable earnings in the prior year. Total IA contributions are equal to the net income for OASI for the prior year (i.e., the increase in the OASI Trust Fund assets from the beginning to the end of the prior year). However, aggregate contributions would be limited to 5 percent of the OASDI taxable payroll.

Aggregate contributions would be divided by the OASDI taxable payroll for the prior year, and this percentage of prior year taxable earnings will be credited to each worker's account. If OASDI net income for the prior year is zero or negative, no IA contributions will be credited.

Beginning in 2044 (or whenever, after 2040, the OASI annual balance becomes positive), redirect any excess of OASI tax income over OASI cost to finance a portion of the IA contributions. The balance of specified IA contributions will continue to be provided from the General Fund of the Treasury.

Accumulations in the IAs would be required to be distributed as a CPI-indexed annuity at initial entitlement to OASI retirement, aged spouse, or aged surviving spouse benefit.

(4) For workers who have had contributions to an IA during their working lifetime, expected lifetime OASI retirement and aged survivor benefits would be reduced by the amount of their IA contributions, accumulated at the rate provided by long-term U.S. Bonds held by the trust funds.

The percentage reduction for benefits paid based on a worker's earnings would be determined at the time of initial entitlement for retired worker or aged surviving spouse benefits based on the worker's earnings. All OASI benefits paid based on the worker's earnings after this point would be reduced by the ratio of the hypothetical accumulation of PRSA contributions to the present value of expected future benefits at the time of initial entitlement (discounted for present value at the yield for special bonds held by the OASDI trust funds).

This IA provision is intended to provide a financial advantage to workers who will have the opportunity to invest the IA in equities and corporate bonds, as well as Government bonds, thus having the possibility of achieving a higher average interest rate than realized by the OASI and DI Trust Funds. Whether workers realize an advantage from the PRSA accounts will depend upon whether they achieve yields on their PRSAs, both before and after retirement, that are at least the level specified for the benefit reduction provision, i.e., the yield on special-issue United Stated bonds held by the trust funds.

Include the entire proceeds of the annuitization of the IA (required as a CPI-indexed annuity at initial entitlement to OASI retirement, aged spouse, or aged surviving spouse benefit) in the amount subject to personal income tax as OASDI benefits. Revenue from personal income tax on the distributions would be transferred to the OASDI and HI trust funds in the same manner as for revenue from taxes on OASDI benefits under current law.

For workers with AIME below $1,150 (this is a 1998 level and would be indexed by the SSA average wage indexing series, AWI, from 1998 to year of initial benefit eligibility) the benefit offset is reduced depending on AIME level. No offset would apply to those with AIME of $650 (1998 level) or less (indexed by AWI). The cost of reducing or eliminating the benefit offset for lower-earning workers would be born by the General fund of the Treasury.

Long-Range OASDI Financial Effects

The combined effect of enacting the basic provisions to modify OASDI benefits, provisions 1a through 1d, would increase (improve) the long-range OASDI actuarial balance by an estimated 0.61 percent of OASDI effective taxable payroll. The complete proposal, including provisions 2 through 4, along with provisions 1a through 1d, would be expected to improve the OASDI actuarial balance by 2.72 percent of taxable payroll. The resulting OASDI actuarial balance would be estimated at 0.65 percent of payroll, and the level of OASDI trust fund assets would generally rise as a percentage of annual cost, reaching an expected 900 percent of annual cost by around 2072. See table 1 details.

The additional revenue required to assure full payment of DI program benefits would increase from 0.22 percent of OASDI taxable payroll for 2014 to 0.63 percent for 2015, and then generally increase to 0.73 percent by around 2072. Amounts equal to these percentages of OASDI taxable payroll would be transferred from the General Fund of the Treasury to the DI program. See table 1.

The total contribution to the IAs would start at about 3 percent of OASDI taxable earnings in 2001, reflecting the excess of total OASI income (including interest) over cost for the prior year. The total contribution would be adjusted as the relationship between OASI income and cost changes over time, reaching a low point of 2.01 percent for 2034. After 2034, the total contribution is expected to rise, reaching the maximum level of 5 percent by about 2058. The portion of the total IA contribution that would be financed by redirecting a part of the OASI payroll tax rate of 10.6 percent would be expected to start at 0.06 percent for 2044, and would be expected to be increased gradually, reaching 1.53 percent by 2073.

It should be noted that the column in table 1 labeled "Total OASDI Contrib Rate" includes the value of General fund transfers to the DI program and excludes the part of the payroll tax that would be redirected to the IAs. The actual OASDI payroll tax rate realized by workers would continue to 12.40 percent (6.20 percent for employees and employers, each).

Stephen C. Goss
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Alice H. Wade
Actuary

Attachment

Sanford 6/8 Memo

Table 1 a Rep. Mark Sanford: IA Contrib = OASI TF Incrs (part from OASI 20 IA Cntrb 4 %, Ben Offset 100.0 %

With Ult Real TF Int Rate of 3.0

With Ult Real IA Yld Rate of 3

With Annuity Net Yld Rate 3

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASI cntrb to IA	Total OASDI Contrib Rate	Gen Fund Trans to DI	Total IA Contrib Rate
1999	10.79	12.70	1.91	194			12.40		0
2000	10.79	12.65	1.86	217			12.40		0
2001	10.95	12.68	1.73	235			12.40		2.93
2002	11.02	12.58	1.67	254			12.40		2.43
2003	11.07	12.69	1.61	272			12.40		2.47
2004	11.14	12.69	1.56	288			12.40		2.54
2005	11.20	12.70	1.50	303			12.40		2.60
2006	11.27	12.71	1.44	317			12.40		2.68
2007	11.34	12.72	1.37	330			12.40		2.76
2008	11.42	12.72	1.30	343			12.40		2.85
2009	11.53	12.73	1.20	354			12.40		2.93
2010	11.64	12.74	1.11	365			12.40		3.00
2011	11.75	12.75	1.00	375			12.40		3.06
2012	11.89	12.78	0.87	384			12.40		3.12
2013	12.04	12.77	0.73	392			12.40		3.18
2014	12.21	13.00	0.80	399	0.22		12.62	0.22	3.21
2015	12.38	13.43	1.04	406	0.41		13.03	0.63	3.40
2016	12.57	13.45	0.88	415	0.01		13.04	0.64	3.77
2017	12.77	13.47	0.69	423			13.04	0.64	3.73
2018	12.98	13.48	0.50	429			13.04	0.64	3.66
2019	13.21	13.49	0.28	433	-0.01		13.03	0.63	3.57
2020	13.44	13.60	0.06	436	-0.01		13.02	0.62	3.44
2021	13.69	13.52	-0.17	435			13.02	0.62	3.30
2022	13.92	13.55	-0.37	436	0.01		13.03	0.63	3.14
2023	14.15	13.58	-0.57	435	0.01		13.04	0.64	3.01
2024	14.37	13.61	-0.76	433	0.01		13.05	0.66	2.87
2025	14.57	13.65	-0.92	430	0.02		13.07	0.67	2.74
2026	14.74	13.68	-1.06	427	0.01		13.08	0.68	2.62
2027	14.89	13.70	-1.18	424	0.01		13.09	0.69	2.52
2028	15.00	13.72	-1.28	421			13.09	0.69	2.42
2029	15.08	13.72	-1.36	419	-0.02		13.07	0.67	2.33
2030	15.13	13.70	-1.42	418	-0.03		13.04	0.64	2.22
2031	15.16	13.70	-1.48	414	-0.02		13.02	0.62	2.13
2032	15.17	13.69	-1.47	412	-0.02		13.00	0.60	2.06
2033	15.15	13.70	-1.44	411			13.00	0.60	2.01
2034	15.09	13.71	-1.39	410	-0.01		12.99	0.59	2.01
2035	15.01	13.72	-1.29	411			12.99	0.59	2.05
2036	14.91	13.72	-1.18	413			12.99	0.69	2.12
2037	14.79	13.73	-1.05	416			12.99	0.59	2.22
2038	14.85	13.73	-0.92	420	-0.01		12.98	0.58	2.34
2039	14.51	13.74	-0.77	426			12.98	0.58	2.47
2040	14.36	13.76	-0.60	433	0.01		12.99	0.59	2.63
2041	14.20	13.77	-0.43	442	0.01		13.00	0.80	2.82
2042	14.05	13.80	-0.25	452	0.02		13.02	0.62	3.04
2043	13.91	13.83	-0.09	483	0.02		13.04	0.64	3.27
2044	13.78	13.78	0.00	478	-0.05	0.06	12.99	0.85	3.61
2045	13.68	13.68	0.00	490	-0.13	0.20	12.88	0.66	3.68
2046	13.53	13.54	0.00	504	-0.13	0.36	12.73	0.69	3.78
2047	13.42	13.43	0.00	518	-0.12	0.48	12.61	0.69	3.87
2048	13.32	13.33	0.00	532	-0.11	0.60	12.50	0.70	3.96
2049	13.23	13.23	0.00	547	-0.10	0.70	12.40	0.70	4.08
2050	13.15	13.15	0.00	561	-0.09	0.81	12.31	0.72	4.16
2051	13.09	13.08	0.00	675	-0.08	0.89	12.23	0.72	4.25
2052	13.04	13.03	0.00	589	-0.06	0.96	12.17	0.73	4.35
2053	13.00	13.01	0.00	602	-0.04	1.00	12.13	0.73	4.46
2054	12.97	12.98	0.00	616	-0.04	1.05	12.09	0.74	4.57
2055	12.95	12.95	0.00	630	-0.04	1.10	12.05	0.75	4.68
2056	12.93	12.93	0.00	643	-0.03	1.13	12.02	0.75	4.78
2057	12.92	12.92	0.00	657	-0.02	1.14	12.00	0.74	4.89
2058	12.91	12.91	0.00	671	-0.02	1.16	11.98	0.74	5.00
2059	12.90	12.91	0.00	684	-0.02	1.17	11.98	0.73	5.00
2060	12.90	12.90	0.00	699	-0.02	1.18	11.94	0.72	5.00
2061	12.89	12.89	0.00	713	-0.02	1.20	11.92	0.72	5.00
2062	12.88	12.88	0.00	728	-0.02	1.21	11.90	0.71	5.00
2063	12.86	12.86	0.00	743	-0.02	1.22	11.88	0.70	5.00
2064	12.85	12.85	0.00	759	-0.02	1.26	11.88	0.71	5.00
2065	12.84	12.84	0.00	776	-0.02	1.26	11.84	0.70	5.00
2066	12.82	12.82	0.00	792	-0.03	1.29	11.81	0.70	5.00
2067	12.80	12.80	0.00	809	-0.02	1.32	11.79	0.71	5.00
2068	12.79	12.78	0.00	826	-0.03	1.35	11.76	0.71	5.00
2069	12.77	12.77	0.00	844	-0.02	1.37	11.74	0.71	5.00
2070	12.74	12.74	0.00	862	-0.03	1.40	11.71	0.71	5.00
2071	12.72	12.72	0.00	881	-0.03	1.44	11.68	0.72	5.00
2072	12.70	12.70	0.00	901	-0.03	1.48	11.65	0.73	5.00
2073	12.67	12.67	0.00	921	-0.03	1.51	11.62	0.73	5.00
2074	12.65	12.68	0.00	939	-0.02	1.53	11.60	0.73	5.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	13.04	13.69	0.65	2.72

Based on Intermediate Assumptions of the 1999 Trustees Report

With Ult Real Int Rate of 3.00

* Net of Benefit Offset/Clawback

Office of the Actuary

Social Security Administration

June 8, 1999

Social Security Administration
June 5, 1999

Harry C. Ballantyne, Chief Actuary

Memorandum

Refer To: TCC

Subject: Estimated Long-Range OASDI Financial Effect of Proposal by Representative Nick Smith—INFORMATION

This memorandum provides the estimated effect on long-range OASDI financial status of an update of the "Social Security Solvency Act of 1995." Specifications for the update have been provided by Kurt Schmautz of Representative Smith's staff.

This proposal would (1) modify OASDI benefits, (2) distribute any excess of OASDI income over cost, each year, to workers for investment in Personal Retirement Savings Accounts (PRSAs), (3) transfer specified amounts from the Treasury to OASDI for years 2001–2009, and (4) reduce each worker's OASI benefits, by an amount equal to the value of PRSA contributions accumulated at a specified interest rate.

The balance of this memorandum provides a description of the proposals and estimates of the long-range financial effects of the proposal on the OASDI program. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

Summary of Proposal Provisions

(201) Raise the normal retirement age (NRA) at the rate of 2 months per year beginning in the year 2000, until reaching an NRA of 67 for persons attaining age 62 in 2011 (eliminate the hiatus in current law). After 2011, index the NRA to maintain the ratio of expected retirement years (life expectancy at NRA) to potential work years (NRA minus 20) at the level for 2011.

(202) Modify the PIA benefit formula by adding a new, third bend point in 2000 equal to $3,720. Set the PIA factor to be applied above the new third bend point at 15 percent for 2000, 13 percent for 2001, 11 percent for 2002, 9 percent for 2003, 7 percent for 2004, and 5 percent for 2005. Index the second and third bend points by the increase in the CPI after 2000 (rather than by the increase in the average wage). Gradually reduce the 32 percent PIA factor by 2 percent per year (multiply by 0.98 each year) after 2000, the 15 percent factor by 2.5 percent per year (multiply by 0.975 each year) after 2000, and the 5 percent factor by 2.5 percent per year (multiply by 0.975 each year) after 2005.

The combined effect of the declining PIA factors and the reduced indexing of the upper two bend points, would be to gradually move toward a PIA formula that would ultimately, in 1999 dollars, pay 90 percent of AIME up to $505 and nothing above that AIME level. This would ultimately be very nearly a flat benefit formula, providing a PIA of about $454 per month, in 1999 dollars, for the large majority of beneficiaries.

(203) Send annual statements to each worker and beneficiary over age 18 indicating the total amount of employee and employer contributions made to date, with interest, and the total amount of benefits received to date, with interest.

(205) Cover all State and local government employees (except full-time students) newly hired in 2001 or later.

(206) Increase the level of benefit paid to all aged surviving spouses by 10 percent beginning in 2001. This provision would for the purpose of retired worker or aged surviving spouse benefits payable to the surviving spouse of a married couple, increase the PIA upon which the benefit is paid by 10 percent. This increase would apply to all qualifying widow(er)s receiving benefits in 2001 and later.

(207) Require the Social Security Administration to study the feasibility of making participation optional.

(101) Starting in 2001, provide for contributions to Personal Retirement Savings Accounts (PRSAs) for each OASDI covered worker who is under age 65 on January 1, 2001. Access to the accumulations in the PRSA would not be allowed until the worker, or surviving spouse reaches retirement age and begins receiving retired worker of aged surviving spouse benefits.

(102) Contributions to PRSAs would be made by redirecting a portion of the OASDI payroll tax from the trust funds to the PRSAs. For years 2001–36, 2.6 percent of each workers taxable earnings would be redirected. After 2036 the portion

of total payroll tax contributions to be redirected would be set annually based on the amount of OASDI total income that would not be needed in order to maintain solvency of the OASDI program on a pay-as-you-go basis with a trust fund ratio of about 50 percent of annual cost.

Transfers from the General Fund of the U.S. Treasury would be required for years 2001 through 2009, with the amounts specified in law as $11 billion for 2001, $59 billion for 2002, $51 billion for 2003, $68 billion for 2004, $79 billion for 2005, $116 billion for 2006, $134 billion for 2007, $146 billion for 2008, and $165 billion for 2009. These amounts are based on current estimates by the Congressional Budget Office of the amount of on-budget surplus for these years.

(103) For workers who have had contributions to a PRSA during their working lifetime, expected lifetime OASI retirement and aged survivor benefits would be reduced by the amount of their PRSA contributions, accumulated at a specified rate. Benefits for disabled workers would not be reduced prior to retirement age because access to the PRSA would not be allowed until retirement age. This hypothetical accumulation would reflect amounts contributed to the PRSA, plus interest as if the PRSA had been invested at the specified interest rate. The specified interest rate would be the rate provided by long-term U.S. Bonds held by the trust funds plus 0.7 percentage point.

The percentage reduction for benefits paid based on a worker's earnings would be determined at the time of initial entitlement for retired worker or aged surviving spouse benefits based on the worker's earnings. All OASI benefits paid based on the worker's earnings after this point would be reduced by the ratio of the hypothetical accumulation of PRSA contributions to the present value of expected future benefits at the time of initial entitlement (discounted for present value at the yield for special bonds held by the OASDI trust funds plus 0.7 percentage point).

This PRSA provision is intended to provide a financial advantage to workers who will have the opportunity to invest the PRSA in equities and corporate bonds, as well as Government bonds, thus having the possibility of achieving a higher average interest rate than realized by the OASI and DI Trust Funds. Whether workers realize an advantage from the PRSA accounts will depend upon whether they achieve yields on their PRSAs, both before and after retirement, that are at least the level specified for the benefit reduction provision, i.e., the yield on special-issue United Stated bonds held by the trust funds plus 0.7 percentage point.

All distributions from PRSAs would be taxed like current OASDI benefits. Revenue from personal income tax on the distributions would be transferred to the OASDI and HI trust funds in the same manner as for revenue from taxes on OASDI benefits under current law.

Long-Range OASDI Financial Effects

The combined effect of enacting the basic provisions to modify OASDI benefits and coverage, sections 201 through 207, would increase (improve) the long-range OASDI actuarial balance by an estimated 3.21 percent of OASDI effective taxable payroll. The complete proposal, including sections 101 through 103, along with sections 201 through 207, would, by design, bring down and then limit the size of the OASI and DI combined Trust Funds to the level of a very minimal contingency reserve (about 50 percent of annual cost), thus reducing the actuarial balance to about zero. See tables 1 and 2 for details.

The portion of the total OASDI payroll tax rate of 12.4 percent that is redirected from the trust funds each year to the Personal Retirement Savings Accounts (PRSAs) of current workers is determined so that the OASDI combined Trust Funds would be expected to decline as a percent of annual program cost through 2036, and would be maintained at a minimal contingency reserve level after 2036. PRSA contributions for each year result in subsequent benefit reductions for those who were working in the current year. These reductions decrease the cost of the program below the level indicated for provisions 201 through 207 alone, thus permitting increasing PRSA contributions for workers in later years.

By 2073, payments of benefits from the OASI fund would be largely eliminated through the PRSA offset, because the career PRSA contributions, accumulated at the long-term U.S. bond rate plus 0.7 percentage point, would exceed the present value of expected benefits (discounted at the same rate) for most retirees and survivors. It should be noted that benefits to disabled workers would be reduced by the modified benefit formula, but would not be offset because the PRSA account would not available until retirement age is achieved.

STEPHEN C. GOSS
Deputy Chief Actuary

Attachments

¯Nsmith 6/5 Memo

Table 1 a Rep. Nick Smith: PRSA Contribution 2.6% to 2038; GF Trans 2001-9 IA Cntrb 2.6 %, Ben Offset 100.0 %

With Ult Real TF Int Rate of 3.0
With Ult Real IA Yld Rate of 3.7
With Annuity Net Yld Rate 3.7

Year	Cost Rate*	Income Rate**	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	IA Contrib Rate
1999	10.79	12.70	1.91	194		12.40	0
2000	10.79	12.65	1.86	217		12.40	0
2001	11.12	10.38	-0.76	231	0.28	10.08	2.60
2002	11.18	11.52	0.35	227	1.16	11.24	2.80
2003	11.20	11.28	0.08	233	-0.25	10.99	2.80
2004	11.23	11.81	0.38	236	0.33	11.32	2.60
2005	11.24	11.79	0.54	241	0.17	11.48	2.60
2006	11.25	12.47	1.21	247	0.67	12.16	2.60
2007	11.26	12.71	1.45	259	0.24	12.40	2.80
2008	11.27	12.82	1.55	274	0.10	12.50	2.60
2009	11.28	13.03	1.75	289	0.21	12.70	2.60
2010	11.30	10.13	-1.18	307	-2.90	9.80	2.60
2011	11.32	10.14	-1.18	299		9.80	2.60
2012	11.36	10.15	-1.21	292		9.80	2.60
2013	11.41	10.15	-1.25	284		9.80	2.60
2014	11.48	10.16	-1.30	276		9.80	2.60
2015	11.53	10.17	-1.35	287		9.80	2.60
2016	11.58	10.18	-1.40	259		9.80	2.80
2017	11.64	10.19	-1.45	250		9.80	2.60
2018	11.71	10.20	-1.51	240		9.80	2.80
2019	11.78	10.21	-1.57	230		9.80	2.60
2020	11.86	10.22	-1.83	220		9.80	2.60
2021	11.95	10.24	-1.72	209		9.80	2.60
2022	12.03	10.25	-1.78	197		9.80	2.60
2023	12.11	10.26	-1.85	185		9.80	2.60
2024	12.17	10.27	-1.90	172		9.80	2.60
2025	12.22	10.29	-1.93	159		9.80	2.60
2028	12.22	10.30	-1.93	147		9.80	2.60
2027	12.21	10.31	-1.91	134		9.80	2.60
2028	12.17	10.32	-1.85	122		9.80	2.60
2029	12.09	10.32	-1.77	109		9.80	2.60
2030	11.98	10.33	-1.85	98		9.80	2.60
2031	11.85	10.34	-1.51	87		9.80	2.60
2032	11.70	10.34	-1.35	77		9.80	2.80
2033	11.52	10.35	-1.17	68		9.80	2.80
2034	11.32	10.35	-0.97	60		9.80	2.60
2035	11.10	10.36	-0.74	54		9.80	2.60
2036	10.87	10.38	-0.51	49		9.80	2.60
2037	10.83	10.38	-0.25	46		9.82	2.58
2038	10.38	10.14	-0.24	46		9.57	2.83
2039	10.12	9.88	-0.24	46		9.32	3.08
2040	9.85	9.82	-0.23	45		9.06	3.34
2041	9.58	9.35	-0.22	45		8.79	3.61
2042	9.31	9.09	-0.21	45		8.53	3.87
2043	9.04	8.83	-0.21	45		8.27	4.13
2044	8.78	8.58	-0.20	45		8.01	4.39
2045	8.52	8.32	-0.19	45		7.76	4.65
2046	8.26	8.07	-0.19	44		7.50	4.90
2047	8.00	7.82	-0.18	44		7.24	5.16
2048	7.75	7.57	-0.18	44		7.00	5.40
2049	7.50	7.33	-0.17	45		6.75	5.65
2050	7.26	7.10	-0.17	45		6.52	5.88
2051	7.03	6.87	-0.18	45		6.29	8.11
2052	6.81	6.86	-0.16	45		6.08	8.34
2053	6.60	6.45	-0.15	45		5.85	8.56
2054	8.39	6.24	-0.15	45		5.64	6.78
2055	6.18	6.03	-0.14	45		5.43	6.97
2056	5.97	5.83	-0.14	45		5.22	7.18
2057	5.76	5.83	-0.13	45		5.01	7.39
2058	5.55	5.42	-0.13	45		4.80	7.60
2059	5.35	6.22	-0.13	48		4.59	7.81
2060	5.14	5.02	-0.12	46		4.38	8.02
2081	4.93	4.81	-0.12	46		4.16	8.24
2082	4.73	4.61	-0.11	47		3.96	8.44
2083	4.52	4.41	-0.11	48		3.75	8.65
2064	4.32	4.22	-0.11	48		3.55	8.85
2065	4.13	4.02	-0.10	49		3.35	9.05
2088	3.94	3.84	-0.10	50		3.15	9.25
2087	3.76	3.88	-0.10	51		2.98	9.44
2088	3.58	3.49	-0.09	51		2.78	9.62
2089	3.42	3.33	-0.09	52		2.60	9.80
2070	3.18	3.09	-0.09	54		2.36	10.04
2071	2.93	2.85	-0.09	57		2.11	10.29
2072	2.89	2.80	-0.08	60		1.86	10.54
2073	2.43	2.35	-0.08	85		1.60	10.80
2074	2.23	2.15	-0.08	68		1.40	11.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	9.98	9.97	0.00	2.06

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback

Office of the Actuary
Social Security Administration
June 4, 1999

Table 2. Estimated Long-Range OASDI Financial Effect of Proposal of Representative Nick Smith

	Section	Estimated Change in Long-Range OASDI Actuarial Balance [1] (percent of payroll)
201.	Raise the NRA by 2 months per year for those age 62 in 2000 to 2011, then index to maintain a constant ratio of expected retirement years to potential work years.	0.50
202.	Provide a third PIA bend point in 2000 with a 5 percent factor; index the second and third bend points by the CPI and gradually phase down the 32, 15 and 5 percent factors after 2000.	2.89
203.	Annual statements for workers and beneficiaries.	([2])
205.	Cover under OASDI all State and local government employees hired after 2000.	0.21
206.	Increase benefit payable to all surviving spouses by 10 percent beginning 2001.	−0.30
207.	SSA study the feasibility of optional participation.	([2])
	Subtotal for sections 201,202,203,205,206,207.	3.21
101.	Set up PRSA accounts starting 2001..	
102.	Redirect 2.6 percentage points of OASDI payroll tax to PRSAs for 2001–2036. After 2036, redirect to PRSAs any OASDI income in excess of the amount needed to cover annual program costs and maintain a minimal contingency reserve trust fund. Transfer specified amounts from the Treasury to OASDI for years 2001–9 (based on current CBO surplus est)..	
103.	Reduce OASI benefit levels by the amount of lifetime PRSA contributions, accumulated at the yield on trust fund assets plus 0.7 percent. ...	−1.15
	Total for proposal.	2.06

[1] Estimates for individual provisions exclude interaction.
[2] Negligible, i.e., less than 0.005 percent of payroll. Based on the intermediate assumptions of the 1999 Annual Trustees Report.

June 5, 1999 Office of the Chief Actuary Social Security Administration

Chairman ARCHER. Our first witness is a Member of the Committee, the gentleman from California, Mr. Stark. And we are happy to hear from you as to your plan. And under the 10-minute rule that I have just stated, you are recognized, and we are pleased to have you out there in the witness stand.

STATEMENT OF HON. FORTNEY PETE STARK, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. STARK. Well, thank you, Mr. Chairman. I was wondering if we could make a deal about questions, anticipating that you and I will be reversing seats here later on in this hearing, and I do appreciate your calling the hearing. And I certainly appreciate your generosity in the time limit.

I have, as usual, my concise 2-minute statement, which will take me at least 10 minutes to deliver. And so your forbearance is appreciated.

I introduced what should become the baseline of these hearings—legislation to preserve and protect the Social Security system for current and future generations. Today's young people want to be

able to rely on Social Security the way their parents and grandparents have. My plan would accomplish this goal without reducing Social Security benefits, without increasing taxes, and it has been scored by the actuaries as achieving the 75-year, long-range solvency.

It would fully protect the Social Security cost of living adjustment, guarantee full benefits for current and future retirees and for women and children and people with disabilities. It is a very simple plan. It would transfer an amount equal to 2.07 percent of the taxable payroll, the size of the current shortfall in Social Security, from the general revenues into the Social Security Trust Fund. It is actually identical to the Archer-Shaw plan, except that it strips away the veneer: it gets rid of the quasi-individual accounts created and instead gets right to the basics. It drops the provisions creating nearly 150 million individual accounts to invest in the stock market. It does away with that ruse, there is no pretense of private accounts for people. It does not mislead the public into thinking they own a new private account. It does not create individual accounts, which would later have to be confiscated at retirement in order to fund a benefit no larger than the Social Security benefit the individual would have received under the current program.

Further, this plan does not tell the American worker they own their own account, but then mandate that 60 percent of this virtual account be invested in stocks.

Why bother with creating virtual individual accounts? Why set up a Federal bureaucracy to create more than 150 million accounts? Why run the money through Wall Street so brokers can siphon off their share? Why reduce the accounts by excessive administrative costs?

My plan does not dig the Social Security financing hole deeper by adding extra benefits for the highest income people. Most people, under the Archer-Shaw plan, would receive benefits only as much as under current law. A few high-income people could benefit greatly from the private accounts if they got very lucky in the market.

My plan makes the point that designing a Social Security plan to achieve 75-year solvency is easy. One can reach the 75-year solvency by simply transferring enough funds from general revenue to meet the shortfall in Social Security. That is all there is to it. It achieves the solvency and has a much smaller general fund transfer than one of the Senate plans, for example. Mr. Gramm's plan demonstrates that if you want more funding for Social Security, all you have to do is transfer money.

Unfortunately, our current budget surpluses may not last forever. After the surpluses disappear, it is not clear from whence the money will come. Will there be an increase in taxes? Will there be cuts in Medicare? Will there be increased borrowing from the public?

This bill strips away that complexity, and it is very simple. It is a straightforward way of achieving the 75-year solvency for the Social Security Program. I am looking for cosponsors, and, as I say, it is a bedrock plan. You could amend it. You could cut benefits, and then not have to take so much money out of general revenues.

You could, rather than invest in the stock market, lift the taxable payroll cap, and it would give you an alternative. If we wanted to match this, all we would have to do is increase the interest that we set on the borrowing so the Social Security Trust Fund from 6.5 percent to 11 percent. That money, of course, would come out of general revenues, as it does now. But there just is not any other way. It is a teeter-totter. You can put this end in the air, and that one comes down, or vice versa.

But this plan, to repeat, solves the problems we are talking about without reducing benefits or increasing taxes, and a 75-year solvency. It takes 2.07 percent of the taxable payroll, transferred from general revenues into the Social Security Trust Fund. Now, you can do that any kind of which way you want. You could cut benefits, of course. I am not so sure that I would want to vote for that, but it is a possibility. But there are not any other ways, Mr. Chairman. And I just thought that we ought to set the standard of what we are talking about and the dollars we are concerned about—we have charts that show each year's contribution and some cost a little more in some years, and some cost a little less, but basically, this is what we are talking about in most every plan, and those that cut the benefits would not transfer quite so much money. That is a choice that we have and I suspect we could vote on later.

And I appreciate the opportunity to testify with you this morning. Thank you.

[The prepared statement follows:]

Statement of Hon. Fortney Pete Stark, a Representative in Congress from the State of California

This week I introduced legislation, H.R. 2039, to preserve and protect the Social Security system for current and future generations. The Social Security system has been the bedrock of retirement income for millions of Americans. Today's young people want to be able to rely on Social Security the way that their parents and grandparents have.

My plan would accomplish this goal without reducing Social Security benefits or increasing taxes. It has been scored by the actuaries as achieving 75-year long range solvency. It would fully protect the Social Security cost-of-living adjustment and guarantee full benefits for current and future retirees—and for women, children and people with disabilities.

It is a simple plan. It would transfer an amount equal to 2.07% of taxable payroll—the size of the current shortfall in Social Security—from the general revenues into the Social Security Trust Fund.

My plan is identical to the Archer-Shaw plan, except that it strips away the veneer. It gets rid of the phony individual accounts created by that plan and instead gets down to the basics.

- It drops the provisions creating nearly 150 million accounts to invest in the stock market.
- It strips away the ruse of individual accounts. There is no pretense of private accounts for people. My plan does not mislead people into thinking that they own new private accounts. My plan does not create individual accounts only to confiscate them at retirement in order to fund a benefit no larger than the Social Security benefit the individual would have received under the current Social Security program. Furthermore, my plan does not tell the American worker they own their own account, but then mandate that 60% of this "virtual" account be invested in stocks.
- Why bother with creating "virtual" individual accounts? Why set up a federal bureaucracy to create more than 150 million accounts? Why run the money through Wall Street so that brokers can siphon off their share? Why reduce the accounts by excessive administrative costs?
- My plan doesn't dig the Social Security financing hole deeper by adding benefits for high-income people. Although most people, under the Archer-Shaw plan would

receive benefits only as much as under current law, some high income people could benefit greatly from the private accounts.

My plan makes the point that designing a Social Security plan to achieve 75-year solvency is easy. One can reach 75-year solvency for Social Security by simply transferring enough funds from the general revenue to meet the shortfall in the Social Security program.

My plan achieves 75-year solvency and has much smaller general fund transfers than the Gramm plan, for example. As the Gramm plan demonstrates if you want more funding for Social Security, all you have to do is transfer money.

Unfortunately, our current budget surpluses don't last forever. After the surpluses have disappeared, it is not clear from where the money will come. Will there be an increase in taxes? Will there be cuts in Medicare? Will there be increased borrowing from the public?

My bill strips away the pretense, complexity and deception in other plans. My plan is a simple, straightforward way of achieving 75-year solvency for the Social Security program.

Chairman ARCHER. I thank the gentleman for his testimony, and it certainly is a very straightforward approach to a solution of the Social Security problem. And it certainly is not overly complex, I do not think. I think the way you presented it, it is easy to understand.

I have one question and then I am going to, of course, recognize other Members. Do you have a projection as to what this does to the unified budget surplus over the 75-year period?

Mr. STARK. I—Mr. Chairman, I would presume it would do the same thing as your plan or any others. It takes about the same amount of money out of general revenues, and it would not make much difference one way or the other.

Chairman ARCHER. I would think it would be significantly different than the Archer-Shaw plan because it takes enough out of general revenue in order to finance the Social Security fund for the next 75 years, but it does not buildup any surpluses in the fund, as ours does, which would permit a reduction in the payroll tax of over 4 percent over the long term. And I would guess from the way you have described it that it—that it has a negative impact of some significant consequences on the unified budget surplus. Whereas ours increases the unified budget surplus by over $120 trillion over 75 years; and that is a rather significant difference. But if you do not have that from either CBO or SSA, we can, of course, gain that later and make the comparisons.

Mr. STARK. Mr. Chairman, I am going to keep this as simple as I can. In the transfers from general revenues, this takes a little less money than your bill. It does not have the 25 basis points a year for administration that your bill would require. The idea that you might gain a lot of benefits through a higher return is one of faith, but I have, and I would submit for the record, the list. In the early years, yours starts with 157, and then runs 82, 85, 100. This one runs 78, 80, 89, 100, 106. Some years it is a little higher. Some years, it is a little lower, but what I am about to suggest to you is that the transfers are very, very close in all years, and if you want to transfer money from the general revenues into the stock market and back into the trust fund, you could do it. But I do not know what you achieve.

Chairman ARCHER. Well, I would say to the gentleman, and I am just told by staff that the actuaries at Social Security have been so swamped trying to meet the demands that they did not have time to compute the impact on the unified budget surplus on your plan, but that it will be available to us shortly. And then we have got to go by whatever the official estimates are, not simply by our desires, and we will be able to make that comparison. Thank you.

Any other Member wish to inquire?

Mr. RANGEL. Yes, I would like to——

Chairman ARCHER. Mr. Rangel.

Mr. RANGEL. You know, Mr. Stark, you passed over the innovative part of the Archer-Shaw plan by not giving the beneficiary the opportunity to participate in individual investment accounts. This is important——

Chairman ARCHER. Will the gentleman suspend for just a minute? If we could, because I will be out there tomorrow and will be happy to respond to any detailed comments relative to the Archer-Shaw plan, if we could concentrate today on trying to develop information on the plans of the Members who are presenting their plans, I think it would expedite our hearings. Would that be acceptable to the gentleman? The gentleman will be able to quiz me tomorrow to the fullest extent.

Mr. RANGEL. Well, there must have been some reason why he would have omitted this, Mr. Chairman, and I respect his opinion, because he has tracked your plan except that he has left out the key, challenging, important part, and that is the high-yield investments. Knowing that Peter studied your plan, I wondered whether or not he could share with us why he omitted that?

Mr. STARK. Well, Mr. Rangel, there are no assumptions in this bill in terms of earnings or dollar amounts. The Social Security actuaries indicated that the Archer-Shaw bill if it only earned a real rate of 4.35 percent, it would fail to close the long-range gap. The 5.35 percent figure, assuming that future stocks will earn a rate of return around 7 percent, Mr. Gramm, like the Federal Reserve Board Governor, and the source of the original individual account plan during the 1994–96 Advisory Council, said that that was way too high. So, we did not want you to get into the stock market. We get into guessing which way the wind is going to blow a week from Sunday. And those are projections that I am not sure that your and my and the Chairman's grandchildren want to rely on.

Mr. RANGEL. But still, Archer-Shaw, if there are not these high returns in the stock market, they go back to general revenue, which takes us back to your bill.

Mr. STARK. Precisely. Precisely.

Mr. RANGEL. Thank you, Mr. Chairman.

Chairman ARCHER. The Chair would like to alert the Members that the Chair intends to continue the hearing through the votes, and Members should take advantage of a time to go vote, and then come back. But we want to proceed on a seamless basis.

Mr. Thomas.

Mr. THOMAS. Pete, what I am trying to do in a rough comparison, notwithstanding the various pieces that folk present, is to look at the Social Security actuaries' 75-year program. Part of my concern is that all of us are familiar with the House's 5-year and the Sen-

ate's 10-year budget window, in which we look at 5 or 10 years and then what happens after that is off the chart. In part, I think in some of these plans we are dealing with the 75-year window, and what happens after that is off the chart.

Now, as you and I know in trying to deal with Medicare, 75 years out is an interesting game to play, anyway. But what concerns me—and I need some response so that you could help me understand—what concerns me about the actuaries' 75-year outlook on your plan in terms of annual balance is that, more so than any other, except I guess the Nadler plan, you start out in 1999 with a 3.98 percent positive, and then it goes to 3.94, 3.82, and it basically is a direct reduction until in the year 2020, you are at 0.04 deficit. But then in 2021, you are 0.37 deficit, 0.67, 0.98, 1.26 deficit. Through the decade of the 2030s, you're in the twos, then you're in the threes, and when you get to the 2060s and into the 2070s—for example, 2070, it is 4.21, 4.26, minus 4.31, minus 4.36, minus 4.0. The assumption is that if you got into the 76th, 77th, 80th year, you continue to go downhill in a minus at fairly significant amounts—$41 trillion in the last year alone.

How do you propose to make up that kind of a profile of a roller coaster going downhill? At the 75-year date that we cut it off, my assumption is that roller coaster is going to go right below zero and keep on going.

Mr. STARK. Well, if I had the foggiest idea of what was going to happen in 2075, I would be concerned. But I would hate to deny our grandchildren, who might run for these positions and be here 50 years from now, the chance to solve that problem all by themselves.

I share with you and with Mr. Rangel the idea that projecting 75 years into the future is an interesting exercise, and certainly an art, not a science. But I merely chose to show that through the 2075s, we could meet that goal. If we changed the goal, we would change the numbers. So if you want to keep it through 2175, we would have to go back and calculate another number. But I submit that that is not the issue. A new number could change.

Mr. THOMAS. Well, I understand the 75-year window, but partly our job might be, I would think, to take a look at what occurs during that period. Granted, it may be an art and not a science, but if we are comparing, as the actuary does, the different plans, a proposal that runs a kind of a flat line or a very modest downhill slope would produce a decision far easier for our children or grandchildren to make when they sit in these seats at the time they need to make the decision.

A significantly declining slope produces a far more difficult decision. If we are at the point of attempting to create a structure that does get us there over 75 years, I am wondering why, just at the outset, we would not chose a plan that shows us, as best projections do, a flat outcome after 2075, or only a slight decline versus one that would be a pretty thrilling roller coaster ride if it were, in fact, a roller coaster ride rather than the Social Security Trust Fund.

Mr. STARK. Well, the basic difference is that thinking in an annual percentage gives you a definitive and predictable amount, and basically I suspect that that is what the Chairman's does. It just

interjects the stock market activity in between, because if the stock does not do well enough, the funds will still come out of general revenues, the extra amount, to meet the benefit. So really the same thing could happen to the Chairman's plan or it could be worse if we happen to hit several major downturns in the market between now and then.

Somehow, it seems to me, that dealing with a certainty in this is a better program, or as much certainty as we can. It still seems to me that it is beyond actuarial science to talk about employment, rates of wages, rates of productivity, birth rates—issues that are not necessarily actuarial decisions when we are projecting that far ahead.

Mr. THOMAS. Well, I appreciate the gentlemen's comments, but when we look at charts that compare, it is going to be difficult for us to pick these significant down sides in a clear direction. It may not be accurate, but I think the direction is the one that I would be concerned about, and I thank the gentleman for his plans.

Chairman ARCHER. Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman. We only have 7 minutes left, and I do not know if I will be able to really develop my point in this time, but I will try.

Chairman ARCHER. The gentleman has 5 minutes.

Mr. MATSUI. Right. Two minutes left, though, if I get to the floor. First of all, your proposal does not cut benefits nor does it increase payroll taxes?

Mr. STARK. Not at all.

Mr. MATSUI. And Mr. Thomas raised the issue about long-term stability, and he compared it, to some extent, and perhaps you did too with the Archer-Shaw legislation. And yours does take money from the general fund for that entire 70-year period.

Mr. STARK. That is correct.

Mr. MATSUI. And it is my understanding that it would come to somewhere in the range of $43 trillion.

Mr. STARK. That is correct.

Mr. MATSUI. And I want to make a comparison here, because that is what the discussion is all about between your plan and Archer-Shaw. The problem I think with what Mr. Thomas was suggesting, and I know he has left, so I am little reluctant to mention his name, but is the fact that Archer-Shaw does not really achieve, assuming everything goes right, long-term stability until 2050, another 51 years from now. And, as you suggest, anything can happen in the interim period. So comparing the two, maybe yours does not achieve stability until 2075, if at all. But theirs has that same problem, at least two-thirds of the way into it. Is that my understanding? Can you elaborate on that?

Mr. STARK. That would be my understanding is that we are dealing in my bill with a fixed amount, and a fixed rate that could be changed or adjusted.

Mr. MATSUI. Right. And the reason the Archer-Shaw plan begins to achieve some stability in 2050 and beyond is because essentially what you do is you either eliminate the individual's Social Security benefits, because they have the individual accounts, up to the amount of the individual accounts, or one could argue the other way that it basically confiscates the amount of money in the indi-

vidual account up to the point where it matches the current level of benefits, is that correct?

Mr. STARK. That is correct, and a few people might get a bonus. But it would be presumed that a lot would get the Social Security benefit, because their investment account would not equal the benefits.

Mr. MATSUI. And so what you are suggesting is maybe a more direct way of dealing with this issue?

Mr. STARK. It is just——

Mr. MATSUI. Everybody uses general revenues.

Mr. STARK [continuing]. It is just trying to simplify the amounts that are going in and not complicate or obfuscate this whole idea of somehow thinking that there's a private account that somebody owns when they do not.

Mr. MATSUI. Right.

Mr. STARK. And it creates a lot of illusions about investing in private securities—in private accounts—but they do not really exist.

Mr. MATSUI. Right. Thank you very much.

Mr. STARK. Thank you.

Mr. WELLER [presiding]. The Chair recognizes Mr. McCrery.

Mr. MCCRERY. Thank you. Just for a quick followup. Mr. Matsui is leaving. But the point Mr. Thomas was making was precisely the opposite of the point that Mr. Matsui attempted to make. There is no stability in your plan in the out years. That's the point Mr. Thomas was trying to make.

While you solve by simply infusing the trust fund with general funds to the tune of 2.07 percent per year, starting next year, at the end of the 75-year period, according to the actuary at the Social Security Administration, you will be—the combined Trust Fund will be declining at a rate of 20 percent per year compared to the costs of the program. So Mr. Thomas was trying to illustrate that under your plan, with no further changes, there is actually a pretty big cliff at the end of the 75-year period which necessitates fairly drastic actions——

Mr. STARK. Sort of like cutting gains tax.

Mr. MCCRERY. And increase taxes. No, it is not like that at all. So, I just wanted to clear that up, lest anyone mistake the Stark plan for being one that establishes stability. It does not do anything of the sort.

Mr. STARK. It just. If the gentleman would yield.

Mr. MCCRERY. Of course.

Mr. STARK. It just does exactly what the Archer-Shaw plan does. It only does not presume any returns from gambling in the market. It just sets a rate that is a reliable rate, and because we state it, it has to be paid. You could argue—you could change the timeframe. That is all right with me. Then you just have to make it 100 years, and then the 2.07 would change to some amount, as would the contribution under the Archer-Shaw plan. So, I mean, it is——

Mr MCCRERY. Yes, but therein lies the difference. In order to assure stability, as Mr. Matsui used the term, and under your plan you would have to, in fact, infuse a much higher percentage of general revenues into this Trust Fund; whereas, the Archer-Shaw plan does not do that. In fact, we are able to reduce payroll tax rates

under the Archer-Shaw plan in the out years, because we do achieve stability on that plan.

Mr. STARK. Only on the assumption that the market will go up.

Mr. MCCRERY. That is correct. The gentleman makes a legitimate point. However, if history is any guide, we do not have to worry about the market in this country.

Mr. STARK. But if the market goes down.

Mr. MCCRERY. Achieving less than what is being predicted by the actuaries. So, if you have faith in the market in this country, and I do and I think most of us do, then I think we can safely assume that, over time, it will produce a higher rate of return than government bonds of Treasuries.

Mr. STARK. I do not intend to gamble with my grandchildren's retirement in the stock market.

Mr. MCCRERY. Well, we are—I mean, life is gambling, Mr. Stark. But I think if we are, in fact, dedicated to a free market economy, as I think we are, we—if the stock market goes south, we all go south. But, again, if history is any guide, the stock market is not going south. We are going to continue to be a vibrant economy over time, and it will produce the higher rate of return.

So, you know, you make a legitimate point, but I do not think that it is a compelling one.

Mr. STARK. It would be a historical first, and I have——

Mr. MCCRERY. It would be, yes. I thank the gentleman.

Mr. WELLER. OK, Mr. Collins.

Mr. COLLINS. Mr. Stark, I was delayed upon arriving here for the beginning of this hearing. Can you just kind of walk through again your presentation proposal for the benefit of this one straggling Member?

Mr. STARK. Very simple. It just takes 2.07 percent of the payroll; it transfers it from general revenues into the Social Security Trust Fund. That holds the Social Security Trust Fund solvent for 75 years; does not reduce benefits; and does not increase taxes. Just that.

Mr. COLLINS. Are you talking about an additional add-on two point, or are you talking about a carve out?

Mr. STARK. I'm not. No more tax. I am just talking about taking from general revenues, as the Archer-Shaw plan does, only I put it right in the Social Security Trust Fund—2.07 percent of the payroll, gross payroll.

Mr. COLLINS. But I am confused here, which is not out of the ordinary. You are talking about 2 percent add-on, or 2 percent of the existing FICA tax, or Social Security tax?

Mr. STARK. I am not talking about FICA tax at all. I am talking about taking 2.07 percent of the taxable payroll, the same payroll that we now take about 12 percent and change, take that amount from general revenues, from the Treasury, put it into the Social Security Trust Fund.

Mr. COLLINS. OK, you are talking about an add-on then?

Mr. STARK. Add on to what?

Mr. COLLINS. That is an add-on. Yes. An add-on to the existing FICA tax?

Mr. STARK. No.

Mr. COLLINS. It is not an add-on?

Mr. STARK. No. No. The government——

Mr. COLLINS. Well, I am not——

Mr. STARK. It is transferred by the Treasury.

Mr. COLLINS. You are not adding on to the tax, but you are taking general revenues and adding to them——

Mr. STARK. No, I am not adding it to the tax. The tax, the FICA tax, will remain the same.

Mr. COLLINS. Yes.

Mr. STARK. The Treasury will transfer the money in one lump sum from the general revenues to the trust fund.

Mr. COLLINS. OK. So, you are just putting money into the Social Insurance Fund?

Mr. STARK. Just adding money into the trust fund, right. Just like Archer-Shaw does.

Mr. COLLINS. I am sorry.

Mr. STARK. Just like Archer-Shaw does. It just goes through several hoops. They give it to you for a while. They pretend you hold it, then they take it away from you when you retire and dump it back in the trust fund, so mine just gets there more directly without confusing our beneficiaries.

Mr. COLLINS. Then, basically, what you are doing is you are transferring from other taxpayers, through general fund contribution, to payments to the Social Security Insurance Fund?

Mr. STARK. Precisely.

Mr. COLLINS. Well, in effect, though, is that not 2 percent of current taxation that people are paying it, and no way in—will they ever get relief from? It is like adding 2 more percent to the tax?

Mr. STARK. Not to the payroll tax. It is adding 2 percent—it is taking 2 percent from general revenues. If there is a surplus, it does not add anything. If there is not a surplus, you would either increase the deficit or have to raise income taxes.

Mr. COLLINS. But general revenues are taxes. Those are tax dollars.

Mr. STARK. Right. They are the benefit tax——

Mr. COLLINS. So if you take and you freeze 2 percent of those tax dollars, then that is 2 percent that are frozen from now on——

Mr. STARK. Precisely.

Mr. COLLINS. That no one would ever have an opportunity for relief from.

Mr. STARK. That is right. There is a guarantee, just like we guarantee paying interest on the Federal debt. And we are guaranteeing it in this case to the seniors and future generations; that we are saying we guarantee, as the other plans do. Chairman Archer, Mr. Shaw guarantee they are going to spend the money. They would just route it differently. All the other plans suggest they will use money if need be. So, I am just trying to say this is what it will be without all the bells and whistles, which may make the other plans better for some people, but I am just saying this shows exactly what it is.

Mr. COLLINS. Or supposing the individual did not have a tax liability?

Mr. STARK. No, no.

Mr. COLLINS. This takes that 2 percent——

Mr. STARK. This takes the entire—of the entire amount, Mr. Collins. It does not deal with the individuals at all. It takes a lump sum in the entirety to keep the trust fund solvent.

Mr. COLLINS. So you are not setting up the individual accounts?

Mr. STARK. No, absolutely not.

Mr. COLLINS. You are just continuing this current pace with those same——

Mr. STARK. Continuing the same Social Security Program we have today, and funding it, funding the solvency of the trust fund by making this transfer.

Mr. COLLINS. You are just a—a dollar—money infusion into it?

Mr. STARK. That is correct.

Mr. COLLINS. Putting it on a money IV?

Mr. STARK. That is right, and it is why I say it is the base bill. You could then change it if you chose. You could create anything, but it shows you what we are going to do—how much we are going to spend. You want to cut benefits? We will take a little less money. You want to take a little more money and increase the benefits? if you think that the earnings of the stock market will be higher, we would spend less.

Chairman ARCHER [presiding]. The gentleman's time has expired.

Mr. STARK. But that is—OK.

Mr. COLLINS. OK. Thank you. Thank you, Mr. Stark.

Mr. STARK. Thank you.

Chairman ARCHER. The gentleman's time has expired.

Mr. Hulshof.

Mr. HULSHOF. Thank you, Mr. Chairman. Mr. Stark, in your oral testimony, you cited one of the other plans and the individual accounts created in that plan, and I think the word you used was a quasi-individual account.

In your written testimony, which was part of the record, you use another word to describe those individual accounts. Do you wish to amend your written testimony, or do you stand by it?

Mr. STARK. Let us see if I can—can you tell me the precise wording? I am happy——

Mr. HULSHOF. In the fourth paragraph, you indicate—you describe the individual accounts——

Mr. STARK. Phoney.

Mr. HULSHOF. As phoney.

Mr. STARK. No, I say they are phoney.

Mr. HULSHOF. Would you use that same terminology, for instance, to describe the Universal Savings Account plan as proposed by the President of the United States? Would that, in your estimation, be phoney?

Mr. STARK. No, the Universal Savings Account is something that you would keep. These accounts, you would not keep, and they are interesting, but they are not yours. They are virtual accounts, but they would not insure the benefits of the individuals. They would be donated back to the Treasury, and then they would get the Social Security benefits.

Mr. HULSHOF. Well, let me follow up on that point, because I think you concede, do you not, at the bottom of your first page that there are American taxpayers and workers who would receive more

benefits under the Archer-Shaw plan than they would under the present system, is that true?

Mr. STARK. There are a few, possibly but not conceivably, that would.

Mr. HULSHOF. And would you also concede the point that under the Archer-Shaw quasi-individual accounts that workers would have at least some ability to direct how those accounts would be invested?

Mr. STARK. I don't think so.

Mr. HULSHOF. Would you——

Mr. STARK [continuing]. I think under the—but I would let the author correct me—I believe those are managed by the government, and that is what raises the cost and it costs 25 basis points a year to do it. So——

Mr. HULSHOF. Would you concede the point that the quasi, or, in your words, the phoney individual accounts created by Archer-Shaw, would allow workers who die before retirement to pass those personal savings on to their heirs? Do you acknowledge that point?

Mr. STARK. Yes, but they would not get any more benefit. I mean, again, if that did not equal the Social Security benefit, or could not pay it, it would, again, revert to the Treasury.

Mr. HULSHOF. Does your plan have any of those options or features that I have just described? That is, add retirement benefit, higher benefit, than the current system——

Mr. STARK. It has exactly, Mr. Hulshof, the benefits that exist today, indexed for inflation. It provides for the COLAs. It provides for disability. Everything—all this plan does is show you that it takes 2.07 percent each year to make the current plan, with the current benefits, solvent for 75 years. There is no hidden agenda in it. There is nothing fancy—I mean, that is all it does, and I can understand that people might like to add on to it or subtract from it, to make less money come out of the Treasury, or to give bigger benefits perhaps. I just tried to attempt to keep the current plan. How much would it cost, out of general revenues. That is it.

Mr. HULSHOF. Thank you, Mr. Stark.

Mr. STARK. Thank you, sir.

Mr. HULSHOF. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Ramstad.

Mr. RAMSTAD. Thank you, Mr. Chairman.

Mr. Stark, let me ask you this: In transferring, as I understand that 2.07 percent of taxable payroll from general revenues into the Social Security Trust Fund—that is what you are doing—you are investing all those dollars in government bonds, which have about a 3 percent return rate, is that correct?

Mr. STARK. Well, I guess I am. But, I do not want to mix apples and oranges. They have about a 6 or 6.5-percent rate. The real rate, depending on inflation, may be 3. I do not care which—you use whichever number you want. But, I mean——

Mr. RAMSTAD. But the point is that all of those dollars go into government bonds, as opposed to private investments?

Mr. STARK. Under the current system, that is correct, yes, sir.

Mr. RAMSTAD. Most of the other proposals that I have seen look at investing funds in ways that have better rates of return, and I

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am curious as to why you chose to keep the funds in the option with the lowest rate of return?

Mr. STARK. I think there are a large number of Americans who have a concern. Rightly or wrongly, they were gambling with their money. You have heard the same concern in your town meetings that we are spending the trust fund that is not there. The government bonds—and so I am just suggesting that this is the way to determine the exact amount that we will have to anticipate coming out of general revenues to meet the 75-year target, maintaining current benefits as we know them today.

Now, you could pay a higher interest rate by law. We could—we would have to kick it up to 11 percent, and then we would not have to take anything out of general revenues directly. We would just have to take it out to pay the interest on the bonds.

Mr. RAMSTAD. Well, I understand that, but it just seems to me when, over the last decade, or the last 12 years, the average rate of return for investments in private stocks has been in double digits, and we are getting 2 to 3 percent from government bonds. That is a huge amount of money, a huge discrepancy, and a lot of——

Mr. STARK. I hear that from Merrill Lynch and Dean Witter every day, Mr. Ramstad. They may be right.

Mr. RAMSTAD. It sounds like, Mr. Stark, as a good friend and colleague, for this the first time, you have probably been criticized for being too conservative.

Mr. STARK. Thank you. Yes.

Mr. RAMSTAD. One general theme I hear at hometown meetings that I have had on this important topic—and I think this theme pervades the body politic—is that most people do not want their Social Security taxes raised or benefits cut. I certainly support that line of thought, share that goal.

Now, your bill would transfer what amounts to 2.07 percent of taxable payroll from general revenues into the trust fund each year, annually, right?

Mr. STARK. That is correct.

Mr. RAMSTAD. Does that actually mean you are raising taxes on Social Security, from 12.4 percent to about 14.5 percent?

Mr. STARK. No, no. It just means that it is a commitment to pay from the Treasury directly to the Social Security Trust Fund. It does not run through the payroll tax system at all. And it is just a commitment to transfer revenues——

Mr. RAMSTAD. But is that not, in essence, a tax increase?

Mr. STARK. It depends on whether or not we are running a surplus or not. It could necessitate a tax increase to keep a balanced budget, if for some other reason—we had a war or something. So, there is no question that it puts a strain on the budget, but all the other bills do as well. They just take money out of the general revenue and give it to individuals or give it to the stock market plans. And I am just circumventing some of those in between steps.

Mr. SHAW. Would the gentleman yield on that? I have just one quick question.

Mr. RAMSTAD. I certainly will.

Mr. SHAW. Would this be subject to annual appropriations?

Mr. STARK. No.

Mr. SHAW. How would it be done?

Mr. STARK. It would just be transferred from the Treasury—the same way, for example, under the same rules that we transfer now some of the—I think it is Medicare tax.

Mr. SHAW. With a refundable tax credit, that goes on forever, but I think perhaps we had better check that and see if that would be subject to annual appropriations, which would be a concern——

Mr. STARK. I doubt it very much.

Mr. SHAW [continuing]. I think to all of us.

Mr. RAMSTAD. Reclaiming my time——

Mr. SHAW. Thank you.

Mr. RAMSTAD. Before the light goes out, let me just ask one final question. What happens in those years when there are not surpluses in the general revenues?

Mr. STARK. That depends on Congress. It would either increase the deficit, if they chose not to raise tax revenues to cover the deficit. The same thing that happens if we fight a war or do anything else.

Mr. RAMSTAD. Thank you, Mr. Stark; Mr. Chairman.

Chairman ARCHER. Mr. Doggett.

Mr. DOGGETT. Thank you, Mr. Chairman.

You indicate that your plan will provide for solvency for 75 years. I am wondering why you did not do it for 175 years, and why the 75-year bar is the appropriate one to set here.

Mr. STARK. Well, I think, Mr. Doggett, that this plan is a lot better than the Chairman's, but I am not prepared to battle the Chairman with both arms tied behind my back. If he only has to do his for 75 years, I am not so confident that I can win what I want to do for 150 years, thank you very much. Fair is fair.

Mr. DOGGETT. Well, is it correct that the further you get out, whether it is to 74 years or 174 years, the more speculative it becomes?

Mr. STARK. The more speculative all plans become, basically.

Mr. DOGGETT. Right.

Mr. STARK. Not so much in terms of whether it is the stock market versus fixed income, but the demographics of the world are debatable and not all that predictable.

Mr. DOGGETT. Right.

Mr. STARK. And by that, I mean the wage rates, the number of people working—those issues become pretty fuzzy when you put out that far.

Mr. DOGGETT. I understand you want your plan judged by the same standard as all other plans that are being submitted, but what is your personal view of the wisdom of picking 75 years as the standard by which all plans should be considered?

Mr. STARK. Well, personally, I would not be inclined to go out that far, but it does not—if that is what we are judging all plans by, it is all right. My sense is that somebody will be back here in the next 25 or 30 years making some adjustment, which is the glory I think of the Social Security system and Medicare; is that we do not make it a static system. We do not bury our head in the sand once we have declared solvency. We adjust to the changes in the world, and to the changes in the economy, and to the changes in demographics, and try to provide for our seniors a stable retirement safety net that they can depend upon.

And I think that the Congress is to be credited for having done that reliably since 1935. And I would like to think that, even without you and me, Mr. Doggett, the Congress will be able to go on ahead and provide a security for the elderly in this country for a long time to come.

Mr. DOGGETT. Thank you.

Chairman ARCHER. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman, and still good morning, Mr. Stark. You know, this House has made some decisions so far this year, and, you know, the President, when he did his State of the Union speech, he proposed setting aside 62 percent of the Social Security surplus for Social Security and spending the rest on other things. And this House has made a decision. In fact, there was a bipartisan vote this past week to lock away 100 percent—Social Security surplus—for Social Security and Medicare, and I think that is the right step. And you are referring to town meetings, what we are hearing back home. And I know that has been applauded by the folks back home.

But when the President, in his proposal, talked about 62 percent of Social Security for Social Security, and he also said we should take one-fourth of that surplus and invest it—by the—have the government invest it in the stock market.

Would your plan allow for government-controlled investment in the stock market?

Mr. STARK. It does not provide for that, no.

Mr. WELLER. Is that an approach that you support?

Mr. STARK. I do not support having the basic Social Security plan invested in the stock market. I have no problem if we decide we have the funds to create on top of Social Security additional IRAs or Savings Plans, and I would be particularly happy to see low-income people get some assistance in doing that. But I just feel that the base plan should be—let us call it a fixed-income plan and a fixed-benefit plan, as it is now. My own philosophy is that we should guarantee that.

Then, if you chose to find other ways to help people save, I would be willing to participate in that.

Mr. WELLER. I am confused a little bit. In the statements that you made so far, it appears that you have been opposed to the idea of personal accounts. And you have just stated that——

Mr. STARK. Yes, I——

Mr. WELLER. It is an account——

Mr. STARK. For the base Social Security——

Mr. WELLER. Yes.

Mr. STARK. For the base Social Security system, I do not think you should. If you want to create additional IRAs or Keoghs or those sorts of things, you know, on top that is OK.

Mr. WELLER. Now, as I understand the Archer-Shaw proposal, and, of course, the Chairman is going to present that tomorrow. But as I understand that, that is exactly what his plan does. Is it takes traditional accounts——

Mr. STARK. Well, with some exceptions. You do not own the account.

Mr. WELLER [continuing]. On top of existing Social Security.

Mr. STARK. No, it is a kind of almost account. It is yours if it beats Social Security, but it ain't yours if it does not. Then you get the Social Security. I mean, there is a lot of convolution to get to the basic Social Security benefit for those—for whom their individual account does not provide enough resources to give them their retirement income at the same level it would be under Social Security.

Mr. WELLER. Well, is not that where there is a lot of similarity between the Archer-Shaw plan and the President's USA plan, because they are both additional, essentially, personal accounts in addition to Social Security? Are not they fairly similar in that approach?

Mr. STARK. You know, Mr. Weller, that may be, but I am not here pushing the President's plan. That may surprise you. But I am just trying to present a plan that I think is fairly simple and does the job that we would all like to tell our seniors we have done. And that is protect their benefits and guarantee them—for 75 years, because that has been raised as the mark. And that is what this bill does. It is different. It does not cut benefits, and it does not invest in the stock market. It does not do a lot of things, but it is a—it is kind of what I like to call the baseline bill, and you can then judge what rates of return you would have to get otherwise to match it. You can adjust it any way you want.

Mr. WELLER. Well, focusing specifically on your proposal, and I know my friend, Mr. Collins and Mr. Ramstad, have both raised this issue here. You propose adding additional funds out of the surplus, essentially 2.07-percent increase above the current 12.4 percent that currently goes in there. How much is that in dollar figures?

Mr. STARK. It is approximately the same that the Chairman's—I am going to guess $80 billion running up to $100 billion per year.

Mr. WELLER. A hundred billion a year, so over——

Mr. STARK. Well, not right now, it is $70 billion, $80 billion.

Mr. WELLER. Now, the projected Social Security surplus over the next 10 years is $1.8 trillion.

Mr. STARK. Just a minute. It runs $78 billion, $81 billion, $85 billion, $89 billion, $92 billion, for the next 5 years.

Mr. WELLER. Thanks. So if the surplus runs out, does that mean we will have to have a tax increase to continue that or have to reduce benefits? What do you—what will occur?

Mr. STARK. We would either have to have a tax increase or run a deficit, which is not unknown. Certainly, we did that under Reagan and Bush for years.

Mr. WELLER. Under Clinton and Carter. But, of course, this Congress has put a stop to that. We want a balanced budget. So, if we want to continue with a balanced budget, what do you believe would have to occur when the surplus runs out?

Mr. STARK. Might probably cut defense. That would be my vote. Cut defense.

Mr. WELLER. All righty. I see my time has expired. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Shaw.

Mr. SHAW. I will be brief, Mr. Chairman, because I know we have a lot of people that want to testify and we want to give them our time.

Mr. Stark, I compliment you as well as the other people coming forth with a plan, and even if we do not like it, at least it gives us a source of comparison. And so I think all these plans should be thought through and considered by the Committee.

The big problem that I have with your plan is that by the end of the 75-year period, the funding shortfall in the plan is 4.4 percent of the taxable payroll, which amounts to approximately $41 trillion in 2074. The cumulative cash shortfall between 2020 and 2074 is $72 trillion. And I am looking at the actuary tables, which I assume the Members on both sides of the aisle have. And when you start comparing that plan with all the other plans—I see Senator Breaux out there and Senator Gramm and others; our other colleagues who will be coming in this afternoon—the ones that go into the private sector run positive at a certain point, by frontloading them now in preparing for the future; where yours, continuing on with the present investment plan, it starts off with a just a huge shortfall, and we are simply just passing this off to the next generation.

And when you start talking about the shortfall that is in this plan, that is going to have to be made up with tax dollars. Where these other plans, according to the actuaries, not according to us, but according to the actuaries, by getting into the private sector, whether you do it through direct government investing or whether you do it through individual retirement accounts, it goes positive after a while, and then I think you can say that you are saving Social Security for all time. And you are building up surpluses rather than dragging them down. Would you like to comment on that?

Mr. STARK. Yes. Because the plan you are talking about, your plan, Mr. Shaw, assumes that in the future the stocks are going to earn an average real rate of return of 7 percent, and that is a rosy assumption. That is not an actuarial decision. The actuaries base their——

Mr. SHAW. I do not.

Mr. STARK [continuing]. Base their decision on this 5.35 assumption on earnings, which would take about 7 percent. And I hope that happens. That would be wonderful. But it is not certain. In my bill, it is certain, that is all.

Mr. SHAW. But in the plan that we have before us, that you have presented to us, there is no assumption. We know that this thing is going to go negative. So that is the problem that we have. We rely as far as the actuaries, they rely upon historical data, and carry that forward into the future, and quite frankly, I think that their figures are very conservative.

Mr. STARK. Yes. I do not, Mr. Shaw, and I am not willing to gamble with the future of Social Security on the basis that we are going to pretend the stock market will go up for all time. It never has, and I am just one who thinks that history might repeat itself.

Mr. SHAW. But, Pete, you have to assume, even though we see that your plan does definitely go negative, we have to assume certain interest rates. And perhaps, you know, you can make that same argument that you have to make certain assumption that

these rates are going to be there, too. So, all we can do is rely upon exact figures——

Mr. STARK. We set the interest rates, Clay, in law. We do not set the stock market returns, and I just tried to present a plan which is certain. It may not do everything that people want in the out years, but it is certain.

Now, when you introduce an element of chance into the plan, it is there. I mean, that may be a reasonable, prudent risk. But it is a risk. It is not a certainty, and I just tried to establish this plan to do what I think all agree we want to do: maintain the benefits; keep the plan solvent. And, say, if you are going to do that, this is the base cost. Your plan would require this much money if the market did not hit your projections.

Now, if it hit more, maybe it would require less money. I will spot that. But this plan merely says, here is what it is—bottom line, no ifs or buts. And that is the difference.

Mr. SHAW. And the shortfall is certain?

Mr. STARK. The shortfall is certain, as is the requirement to keep it solvent for 75 years.

Mr. SHAW. And the shortfall in many of these other plans, and I am just not touting the Archer-Shaw plan, there are other plans that are out there. But those do not have the certainty of a shortfall, as yours does.

Mr. STARK. My only feeling is that the rules were set down that we make it work for 75 years. If we would change that to 100 years, that is OK with me—or a 150 years, as Mr. Doggett suggested. Let us do that, and then we will have different rates and different actuarial projections. But 75 years seems an adequate time line to me.

Chairman ARCHER. The gentleman's time has expired. Mr. Stark, thank you for your presentation and for your contribution to this debate.

Mr. STARK. Thank you, Mr. Chairman.

Mr. HERGER. Mr. Chairman.

Chairman ARCHER. Oh, Mr. Herger.

Mr. HERGER. Just to make a point that there has been a lot made about the 75 years. And just looking in the 1999 annual report that was brought out by the Board of trustees for the Social Security. On page 9, it indicates their reason for using 75 years. In summary, at the end of the paragraph, thus a 75-year projection period will include the entire working or retired lifespan of the great majority of workers now contributing to the program, as well as those now receiving the benefits. So I think there is a reason why the Board of trustees used 75 years. This is not something that we have just pulled out of the air. It is something that they decided to use. Thank you, Mr. Chairman.

Chairman ARCHER. I thank the gentleman for his comments, and, of course, that is true. And for those of us who have been around for a number of years, we know that the actuaries have always been charged with the responsibility of projecting for 75 years to determine if the fund is viable, stable, and sound. It might be that number should be increased now that longevity has increased. Perhaps it should go to 80 or 85. But there is a very, very cogent reason for the use of 75, if not more.

The Chair would also observe that this is virtually a zero sum game that we are in. And you can get something apparently and be giving up something that is not apparent. And it is very, very important that all of these plans ultimately, side by side, also have the standard of judgement as to what the impact is on the unified budget surplus. And, unfortunately, we do not have that now for all of the plans from Social Security actuaries. But before too long, we will, and they will need to be put side by side.

Now, let me also say that as a basis for our consideration, all of us may disagree with what the actuaries project. I have done plenty of that myself in the past. We may disagree with what the estimators project when we get into tax relief. I have done plenty of that myself. But in the end, there has to be a "supreme court" by which all of us live and by which our plans are compared. And that "supreme court," in this instance, is the actuaries' projections which they make and which they have the expertise to make. And each plan needs to be compared, side by side, with that.

Now, Senator Gramm, thank you for your patience in waiting through all of the questioning. I know you have done a awful lot of work on Social Security. You are not new to this game, and we are pleased to have you before us. And we are pleased to hear your presentation about your plan.

STATEMENT OF HON. PHIL GRAMM, A U.S. SENATOR FROM THE STATE OF TEXAS

Senator GRAMM. Well——

Chairman ARCHER. Welcome.

Senator GRAMM. Thank you, Mr. Chairman. I want to say that there is no more important subject that anybody in America could talk about, if you are talking about the future of our country, than Social Security. So it was well worth the wait, and I want to thank you for inviting me.

I also want to congratulate you and Mr. Shaw for courageously coming forward with a program. I think when history writes its important chapter on this subject, it is going to deal very kindly with you. It is going to deal very unkindly with President Clinton, in my opinion.

Let me just read from the actuary about the plan I want to talk about, and then I will try to go through some important points on it.

The actuary in scoring the plan that I want to talk about today, says the plan would eliminate the long-range OASDI actuarial deficit. The OASDI Trust Fund would be substantial and rising at the end of the long-term, 75-year period. In other words, the plan I am talking about today solves the problem forever, not just 75 years.

In addition, the trust fund rises every year during this—while this plan is in implementation.

Now, let me first try to just show you a couple of things. I want everybody to look at this chart. The idea of this chart is that we can forget all this silly business about raising taxes and cutting spending to deal with these problems. Now, this first chart deals with Medicare and Social Security. We face both of them. They are the greatest single perils that face the American economy, and the only two really dark clouds on the horizon. But they are really dark

and they are really big. And I presented them as a sort of a gap and a bridge that we have got to fill at two dates: 2020 and 2040.

First of all, if we cut—eliminated defense in 2020, and this is projecting defense as the same share of GDP, we could not fill the gap created by these two entitlement programs. If we eliminated all domestic programs, we could not fill this gap.

By 2040, if you double income taxes, you could not fill this gap. So the idea that there is some little gimmick of transferring revenues from general revenue to a payroll tax trust fund is going to solve that kind of problem is laughable.

Now, what is the solution to the problem? Well, the solution to the problem is very simple. It is powerful, but it is simple. And Einstein said it, the most powerful force in the universe, according to Albert Einstein, is not gravity; is not atomic energy. It is the power of compound interest. It is interesting that Einstein would recognize the power of compound interest as being the most powerful force in the universe for a man who invented the formula $E = MC^2$.

Now, what I want to show is the simple point, and it is important to Chairman Archer and Mr. Shaw's plan. It is important to my plan. First of all, get it out of your head that somehow that there is a rate of return on the Social Security Trust Fund as it now exists. There is no Trust Fund, and there is no rate of return. And think about it this way: when you borrow from yourself is there a rate of return on that loan? No. When the Social Security Administration lends to the Treasury does the Federal Government get a rate of return on that loan? No. There is no rate of return on the Social Security Trust Fund, because there is not real investment made. The power of the Archer-Shaw plan, the power of the plan I am talking about, is it makes a real investment.

Now, if you today take a worker making $30,000 a year paying into the current Social Security system, we are going to be about 30 percent short of paying promised benefits, and they would get $9,061 a year at the end of a working life under the current system.

If you simply took the same money they are going to pay into Social Security, and you invested it conservatively—60 percent in stocks, 40 percent in bonds—at the rate of return we have achieved over the last 75 years, including two World Wars and a Great Depression, you could get an annual payment of $64,060. Now that is the power of compound interest.

It is the only force that gives us any opportunity to deal with this problem. You do not take advantage of that, and you are going to be committed to constantly pitting our children against our parents. If you cut benefits, you hurt the retirement security of your parents. If you raise taxes, whether it is income taxes or payroll taxes, you are diminishing the future of your children. And every year, as this thing goes on, you are going to be forced into this excruciatingly painful choice where America is the loser.

Now, what is the alternative? The alternative is to take advantage of this godsent surplus we have now. If we do not do something about it, we are not going to have it when you need it to pay for these Social Security deficits. But we have it right now. So what can you do with it?

Well, Chairman Archer and Mr. Shaw invest 2 percent of it, and they achieve something extraordinary, and that is, they make the system permanently solvent. But that means that during this interim, we are going to have to redeem the existing Trust Fund. And what does that mean?

That means we are going to have to come up with about $2.5 trillion to pay back the Social Security Trust Fund for all the money we borrowed before the system begins to pay for itself.

Now, if we did this, it would go down as one of the greatest legislative successes in American history, and people would sing songs about this Congress. But please remember that, even if you adopt this plan that we are talking about, we've still got to pay back all this money borrowed from Social Security. It is at least $2.5 trillion.

Now, to get to the point that I want to make, and there is nothing magic about my plan. But it proves something. First of all, what I do is claim the Social Security surplus belongs to Social Security. How dare the CBO say if you take the Social Security surplus and use it for Social Security, then you are changing current services, and you are hurting the general budget. Well, it never was the general budget's money to begin with. It is Social Security's money. So what I say is this: as long as you have got a surplus, whatever amount of it belongs to Social Security, use it for Social Security. And, when your surplus is not as big as Social Security surplus, take the whole surplus for Social Security. It is a simple formula.

Now, here is what you can do doing that. You can let every working American chose, through a professional money manager that would be regulated by a new Social Security Investment Board, to invest 3 percent of their current payroll. So I go 1 percent point higher, and in doing so, I take more of the Social Security surplus.

In addition, in working with the actuaries at Social Security, I determined that 3 percent does not use up the whole Social Security surplus. So, in working with Steve Goss, he kind of came up with the idea what about taking people in the age group 35 to 55, and for those people in that age group do an additional 2 percent that would be dedicated solely to funding their benefits. Doing that, you use up the entire Social Security surplus, which we have and which we are in the process of stealing and squandering every single day. We stole $21 billion of it last year. We have already stolen for next year $7 billion in the emergency supplemental. It will soon be gone if we do not use it.

The point is by doing that, you can achieve the following things. One, you can make Social Security solvent forever.

Number two, you do not have to pay the trust fund back so that you do not have a hidden $2.5 trillion cost in here that kicks in in 2013, and does not go away until about 2060. By making the investments we are talking about, you make the system totally self-financing by 2039.

Now, what I am proposing is an investment-based system that combines the best of both worlds. From private investment, you get things similar to IRAs and 401(k)s that people know. You get the power of compound interest. You get professional money managers.

You get strict financial standards, and you get worker ownership and private property.

From the government system that we know and also love, we get government backing. We get inflation protection. We get guaranteed lifetime benefits. We get family and survivor benefits. And we get progressive benefits.

Final point, and I will quit. There is on my side of the Capitol a sort of a macho that you have got to cut Social Security benefits. Now, I can support cutting them. I can support not cutting them. But the point is the cuts, relative to the power of compound interest, are insignificant. Once you get into the investment system, and the sooner you get into it, and the heavier you get into it, the better it works. Cuts and tax increases become irrelevant. So, my view is we can do it by whacking the cost of living increase. We can do it by means testing. We can do it—you know, any of these cuts you want to do, but do not deceive yourself into thinking that they really solve the problem. They make you feel good—no pain, no gain kind of business. But the point is if you take the resources we have, you have them invested, you solve the problem.

[The prepared statement follows:]

Supplemental Material to Accompany the Statement of Hon. Phil Gramm, a U.S. Senator from the State of Texas

The attached summary provides a section-by-section analysis of the Social Security Preservation Act, an Investment-based Social Security reform plan authored by Senator Phil Gramm. According to estimates prepared by the Social Security Administration, "the plan would eliminate the long-range OASDI actuarial deficit, estimated at 2.07 percent of taxable payroll under present law. The OASDI trust fund would be substantial and rising at the end of the long-range 75-year period." In addition to providing permanent solvency, the plan guarantees each worker 100 percent of the benefits promised by the current system, plus a bonus equal to 20 percent of the benefits funded by their investments.

The Social Security Preservation Act allows each worker to set aside 3 percent of their 12.4 percent Social Security payroll tax, which will be owned by the worker and invested in stocks and bonds by a professional money manager in a "Social Security Savings Account for Employees" or "SAFE Account." The worker can choose from any privately-managed SAFE Account fund certified for safety and soundness by a federal board.

Upon retirement, any worker can opt out of the investment-based system and receive 100 percent of the Social Security benefits guaranteed to them under current law. However, it is expected that most workers will choose to remain in investment-based Social Security and will use the funds in their SAFE Account to purchase a "Savings Annuity For Eligible Retirees" or "SAFER Annuity." The SAFER Annuity will be guaranteed for life and supplemented by the Social Security system if it does not produce a retirement benefit at least equal to 100 percent of the benefits promised under the current system, plus a bonus equal to 20 percent of the payments funded by the SAFER Annuity.

Private companies offering SAFE Accounts and SAFER Annuities will charge all participants a single uniform investment fee, not to exceed 0.3 percent of assets. SAFER Annuities will provide workers of the same age the same monthly benefit relative to the size of their SAFE Account, regardless of sex, race, health status, etc.

Over the next ten years, the Congressional Budget Office projects a Social Security surplus of about $1.78 trillion, while SAFE Accounts funded at 3 percent of OASDI wages would cost about $1.35 trillion, leaving $430 billion in Social Security surpluses. The Social Security Preservation Act uses these remaining surpluses to target additional investment for those age 35–55 in the year 2000, allowing these workers to invest an extra 2 percent of their wages. These extra investments will begin to fund Social Security benefits at the height of the baby boom retirement, providing additional resources in the critical years of the transition. The extra 2 percent will not be counted in calculating the worker's 20 percent bonus, but will be used entirely to fund the benefits they receive from the existing Social Security system.

THE SOCIAL SECURITY PRESERVATION ACT

Section by Section Analysis

SEC. 1—SHORT TITLE AND TABLE OF CONTENTS

SEC. 2—FINDINGS

SEC. 3—ESTABLISHMENT OF INVESTMENT-BASED OPTION FOR SOCIAL SECURITY BENEFITS

Amends the Social Security Act to preserve all existing Social Security provisions (OASDI) in a new Part A and creates a new Part B providing an Investment-Based Social Security option for those workers who voluntarily choose to participate in the investment-based alternative.

Sec. 250 GUARANTEE OF PROMISED BENEFITS

Those opting into the Investment-Based system are guaranteed never to have a benefit less than that promised under the current system, plus a bonus of 20 percent of the benefits paid by their Part B investments.

Sec. 251 DEFINITIONS

Sec. 252 SOCIAL SECURITY SAVINGS ACCOUNTS FOR EMPLOYEES (SAFE ACCOUNTS)

Each current worker may choose to establish a Social Security Savings Account for Employees or SAFE Account. All individuals who will join the workforce in 2000 or later will enter the investment-based system. The worker shall choose the investment fund to professionally manage his SAFE Account from among those investment funds qualified by high standards of safety and soundness, and may change funds once every year. The Account will be the property of the investing worker.

Sec. 253 SAFE INVESTMENT FUNDS

SAFE Accounts will be managed by qualified SAFE Investment Funds, which will be certified and regulated for safety and soundness by the new Social Security Investment Board. Under the parameters set by the Board, the Funds will invest the assets of the SAFE Accounts in stocks, bonds, bank deposits, insurance instruments, annuities and other earnings assets. The Funds will provide an annual report to each participant showing the dollar value of investments over the last quarter, the last year and the life of the SAFE Account. The report shall also project how much each worker will have at retirement if contributions and earnings continue at the same rate during the remainder of his or her working life. Each Fund shall accept all eligible workers requesting to join such Fund. The Fund shall charge all participants a single uniform investment fee as a percent of the investment, not to exceed 0.3% of assets.

Sec. 254 SOCIAL SECURITY INVESTMENT BOARD

Establishes a Social Security Investment Board which will set the general safety and soundness parameters of investments held as part of SAFE Accounts but will be prohibited from requiring or denying the purchase of any specific stock, or in any way dictating which individual investments are made. The Board will protect the safety and soundness of SAFE Investment Funds with the power to order compliance and, where appropriate, decertify and shut down any Fund found to be in violation of Board standards. The Board shall annually provide information on all qualified Funds to workers. The annual report shall include data on the rate of return achieved by each SAFE Investment Fund.

The Board will be comprised of the Secretary of the Treasury, the Chairman of the Federal Reserve Board, the Chairman of the Securities and Exchange Commission and two outside experts with substantial experience in financial matters, who will be appointed by the President and confirmed by the Senate. One of the outside Members will be nominated and confirmed as Chairman.

Sec. 255 SAFE ACCOUNT CONTRIBUTIONS

Workers participating in the investment-based system will initially invest 3 percent of their wages into their individual SAFE Account. The remaining 9.4 percent of the current 12.4 percent paid in Social Security taxes would continue to be used

to pay benefits under the current Social Security system. The 3 percent investment rate will automatically increase in the future as Investment-based Social Security becomes self-financing. In addition, workers age 35–55 in the year 2000 will invest an extra 2 percent of their wages to provide additional resources in the critical years of the transition. The extra 2 percent will not be counted in calculating the worker's 20 percent bonus, but will be used entirely to fund the benefits they receive from the existing Social Security system.

An entry on participating workers' paycheck stubs will show exactly how much money was invested in their SAFE Accounts for that pay period. The payment into the workers' designated account will be made directly from the Social Security Administration at least once a quarter. The Board is empowered to require that investments are made on a more timely basis if more frequent investment is deemed to be feasible.

Sec. 256 SOCIAL SECURITY SAVINGS ANNUITIES FOR ELIGIBLE RETIREES (SAFER ANNUITIES)

Upon retirement, a worker participating in investment-based Social Security will use the funds in his SAFE Account to purchase a Savings Annuity For Eligible Retirees or SAFER Annuity. Under the investment-based system, the SAFER Annuity will be guaranteed for life and supplemented by the Social Security system if it does not produce a retirement benefit at least equal to a) 100 percent of the benefits promised under the current system plus b) a bonus equal to 20 percent of the payments from the SAFER Annuity. This benefit will be fully protected against inflation. Each SAFER Annuity Fund must accept all eligible retirees requesting to join such Fund. SAFER Annuity Funds shall charge all participants a single uniform investment fee, not to exceed 0.3 percent, and shall provide each worker of a particular age the same monthly benefit relative to the size of their SAFE Account, regardless of sex, race, health status, etc.

Early Retirement Option.—Workers can retire at any age and draw their Investment-Based Social Security benefits once they have built up a SAFE Account large enough to fund a SAFER Annuity equal to at least 120 percent of the Social Security benefit promised at the early retirement age and fund any survivor, spousal or other benefits that might be triggered by their retirement.

Unrestricted Right to Use Remaining SAFE Account Assets.—Workers who have built up enough funds in their SAFE Account to finance more than 120 percent of the benefits promised under Social Security and fund any other benefits their family might receive under the current Social Security system may use any remaining SAFE Account funds as they see fit.

Bequests.—If a worker dies prior to retirement, the worker's SAFE Account, minus the present value of benefits promised to the surviving family members under the current Social Security system, will become part of the worker's estate.

Sec. 257 MONEY BACK GUARANTEE

Upon retirement, any worker may choose to opt out of the Investment-Based system and instead receive 100 percent of the benefits he would have received had he stayed in the current Social Security system. Those opting for this money back guarantee will receive monthly benefit checks directly from Social Security. Workers who opt upon retirement to return to the existing Social Security system will forfeit all their SAFE Account assets directly to the Social Security Administration to be deposited into the Social Security Trust Fund.

Sec. 258 GUARANTEE OF PROMISED BENEFITS

A worker whose SAFE Account is not sufficient to purchase a SAFER Annuity which will pay a monthly benefit equal to that promised under the current system plus a bonus of 20 percent of any payments from their SAFER Annuity will receive a supplemental payment from the Social Security Administration. Because this guarantee is based on the inflation-adjusted benefit a worker is promised under the current system, the guarantee fully covers the effects of inflation.

Sec. 259 INVESTMENT RATE INCREASES

Social Security Surplus Investment.—In any year the Social Security Investment Board certifies that the annual Social Security surplus is greater than the amount needed to finance the 3 percent investment rate (and the temporary 2 percent additional investment to help cover the transition), the Board shall automatically increase the investment rate in increments of 1⁄10 of 1 percent, up to a maximum of 8 percent. If, in any year, the annual Social Security surplus is less than the amount needed to fund the 3 percent investment rate, the Social Security Commis-

sioner shall redeem assets of the Trust Fund to ensure that benefits are fully paid and that the investment rate shall never drop below 3 percent.

Social Security Reserve.—The Social Security Investment Board shall ensure that a suitable reserve is maintained in the OASDI Trust Funds.

Sec. 260 TAX TREATMENT OF INVESTMENT BASED SOCIAL SECURITY

SAFE Accounts and SAFER Annuities will build up tax-free until withdrawal. At retirement, payments from a SAFER Annuity up to 120 percent of benefits promised by the current system will be taxed in the same manner as Social Security benefits. Any additional payment, or any lump sum withdrawal, would be taxed as any annuity payment would be taxed under the Internal Revenue Code. The amount of SAFE Account contributions must be shown on a worker's W–2 as well as the worker's payroll receipt.

SEC. 4—PAYROLL TAX REDUCTION RESULTING FROM INVESTMENT-BASED SOCIAL SECURITY

After the investment rate has risen to 8 percent and the necessary portion of the remaining payroll tax is dedicated to fully fund disability insurance, the payroll tax rate shall drop from 12.4 percent to 8 percent plus the rate required to fund disability insurance.

SEC. 5—FINANCING OF INVESTMENT-BASED SOCIAL SECURITY

Recapture of Federal Corporate Income Taxes Arising from SAFE Account and SAFER Annuity Investments.—The Secretary of Treasury, in consultation with the Social Security Investment Board, will annually estimate the amount of corporate income tax revenues that can be attributed to the contributions and accumulated capital buildup in the SAFE Accounts and SAFER Annuities. Within 3 months after the end of each fiscal year, the Secretary of Treasury shall transfer to the OASDI Trust Funds the amount of federal corporate income taxes attributable to the assets held in SAFE Accounts or SAFER Annuities.

In calculating the recapture rate during 2000 and 2001, the Secretary of Treasury shall assume that 80 percent of the total SAFE Account and SAFER Annuity assets are net additions to national investment, that 10 percent of that amount will be invested abroad and not subject to federal taxes, and that 5 percent will be invested domestically but outside the corporate sector. Thus 68.4% of the profits from SAFE Account and SAFER Annuity assets shall be assumed to be net additions to taxable corporate income, resulting in an effective tax rate of 23.9% which will be credited to Social Security.

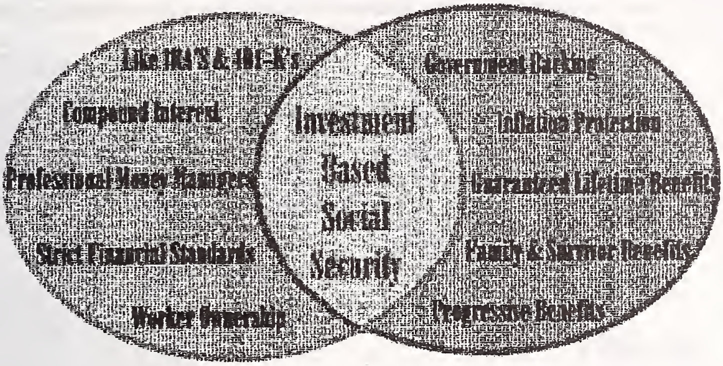
Dedication of Part B Savings to Social Security Trust Fund.—Any other savings resulting from Investment-Based Social Security that flow to the federal government, including increased revenues resulting from federal taxation of SAFER Annuity bonuses and excess SAFE Account distributions, shall be credited to the OASDI Trust Funds.

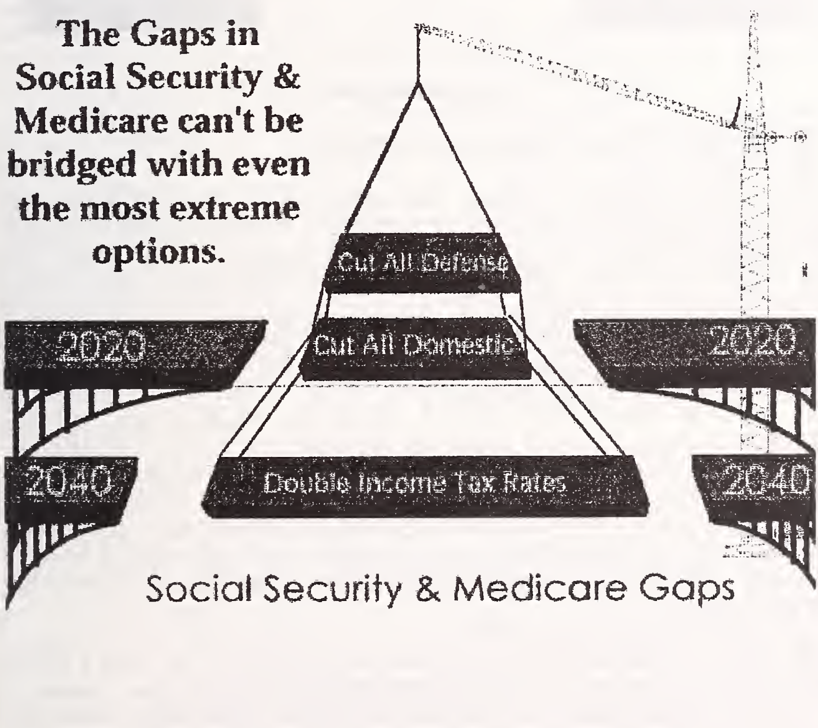
Dedication of Budget Surplus to Saving Social Security.—Each quarter beginning in the year 2000, the Secretary of Treasury shall reimburse the OASDI Trust Funds from the unified budget surplus an amount equal to the actual investments made in SAFE Accounts in that quarter. This reimbursement will be permanently reduced in any year that a reduction can be made without creating a future cash shortfall in OASDI, until the reimbursement is eventually eliminated. To ensure that these budget surpluses materialize, the discretionary spending caps in place under current law are extended through 2009.

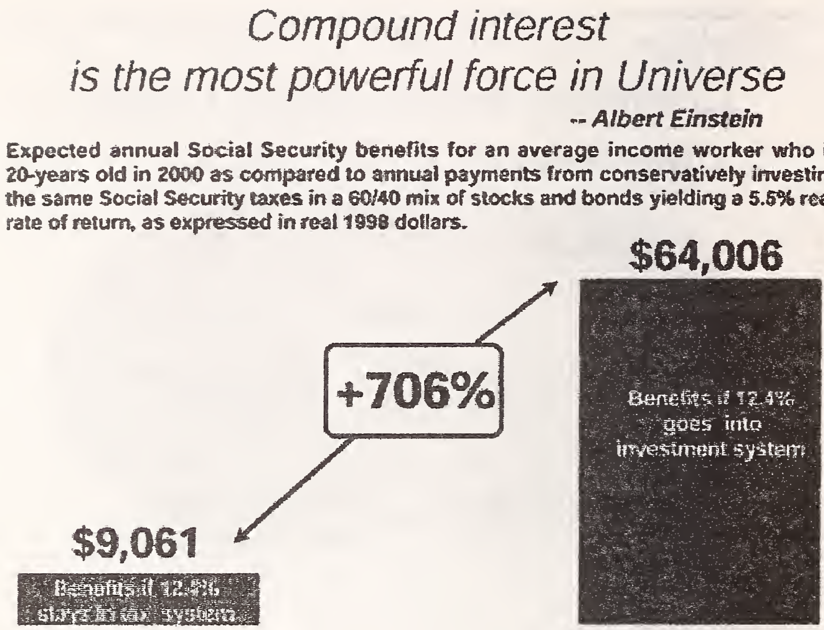
The Solution: *Investment-Based Social Security*

Combining the Best of Both Worlds

Private Investment **&** Social Security







Chairman ARCHER. Thank you, Senator.

Mr. Shaw.

Mr. SHAW. Senator Gramm, thank you for a very fine presentation and a plan that I think is definitely worthy of this Committee's consideration. Interestingly enough, it was only about an hour and a half ago that I asked Kim, our Staff Director on the Social Security Subcommittee, to look into the possibility of what effect it would be of putting different percentages into different age groups in order to try to eliminate or certainly lessen the tax burden which I think all of these plans are going to call for in about the year 2015 to about 2030. And I think you could almost all but eliminate it, and it would certainly increase the amount of the Social Security surplus that we would be using for exactly what it should be used for and that is investment into the Social Security accounts that would be individually held by the American workers.

I also want to compliment you for very much for—and I believe your plan, similar to the Archer-Shaw plan, also has an inheritable feature——

Senator GRAMM. Yes, it does.

Mr. SHAW [continuing]. For workers that don't retire, and I think that is one of the great things about your plan, our plan, and several of the other plans that use the individual retirement accounts. So many of the American workers today—particularly minorities who go into the work force earlier, die younger, and so many of them really never get to enjoy the moneys that have been put aside for them—can't leave it to their family, and they simply lose it.

When Social Security was first put into law some 60 plus years ago, the average age span, I think, was 62 years, and retirement was at 65, and you had so many workers for each retiree, far exceeding what it is today, so the plan worked very well as a pyramid scheme, but that pyramid has certainly narrowed now, and I don't think that anybody would come up with the blueprint we have today for what we have as to workers per retiree. We are enjoying longer life, and we have got to have greater return on our investment and continue to receive the benefits.

I also think that it is never going to happen that this Congress is going to decrease the benefits. I certainly wouldn't support that, and I think particularly when you have a plan, such as yours and such as ours, that doesn't do that. Why do that? I can remember back in the years when I was mayor of Ft. Lauderdale. You summarily think, "Well, we are going to have to just raise our water bill a lot." But when you have people coming in and talking about "That is a loaf of bread for me," at that time you really think, "Geez, there are really people out there that they have got every dime of this spent," and the idea of saying that we are going to take away from our mothers and fathers, even a dime, that is a very significant cut to a great deal of our population. And when we can come up with a plan, too, that will give the disadvantaged in our country an opportunity to accumulate some wealth; that they can look at something that is theirs; that they can participate in ownership and the great capitalistic system that we have today, it would be a shame to walk away from that opportunity.

Senator GRAMM. Well, Mr. Shaw, let me say this: that Social Security is probably the only program in America that redistributes wealth from minorities to whites, and it does it really for two reasons. Number one, minorities tend to start working sooner and since, under our system, nothing you pay into the system until you are 30 years old counts toward your benefit, all of that early work is for all practical purposes lost for them. Whereas, under your plan with the Chairman, under my plan, and under every other investment plan, early work pays big dividends, because you get the compound interest. The second thing is, is the expected lifespan, and by having a death benefit, under my plan and under yours, if you die before you draw out your account, it goes to your survivor, so it becomes a wealth source.

The final point I would like to make is we currently are projecting a $1.78 billion surplus in Social Security. The only way you can convert that money we have now into money we will need later to pay Social Security benefits is to invest it. Now, having one part of government lend it to another part of government in no way makes it available when we need it, because the part of government that borrows it has got to raise taxes or cut spending to pay it back, and so you are just as well off without it than you are with it, but if you can make a real investment, that is how working people every day, through IRAs and 401(k)s, solve this problem. They have got income when they are working; they are not going to have as much income when they retire, so they put money into IRAs, they put money into 401(k)s, and they convert current income into wealth which pays them in retirement—same principle.

Chairman ARCHER. The gentleman's time has expired.

Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman.

Thank you very much, Senator. I appreciate the fact that you have waited about an hour and a half; I know your time is valuable, as well.

You ultimately divert about 5 percent of the payroll taxes to the safe accounts, the individual accounts. Is that my understanding? Once you get beyond 2000——

Senator GRAMM. Well, what we do is the following thing: we take the surplus that belongs to Social Security, and we give it to Social Security, and we allow individuals to make the decision as to which money manager to go with and to make the money. So, what we do, everybody gets the chance to do 3 percent. Anybody can stay in the current system; nobody is forced——

Mr. MATSUI. I understand that, but you are diverting the money to individual accounts or safe accounts.

Senator GRAMM. Yes.

Mr. MATSUI. And knowing that there is an unfunded part of the Social Security system given the 12.4 percent, 14.4 percent differential, you make up the unfunded part of this over the 75 years by putting more general revenues into the fund in order to make up for the loss of revenues because of the 5 percent.

Senator GRAMM. We have a simple formula and it is the Social Security surplus belongs to Social Security. If there is not a general surplus—in other words, if our actual budget surplus is less than the Social Security surplus, then all of the budget surplus belongs to Social Security. But using our current projections under that formula, we can fund the plan because it becomes self-sustaining by 2039, and in fact when the first baby boomer retires, the investments they will have made fund 10 percent of their Social Security benefits. The last baby boomer, when he retires 20 years later, it funds 50 percent of his benefits.

Mr. MATSUI. You will recall in 1981 when we had Dave Stockman testify before this Committee—you were on the Budget Committee at that time in the House—he talked about a rosy scenario, and it is my understanding that you do make a projection of increased revenues into the Treasury based upon the fact that this system will generate additional revenues. In other words, it kind of generates on its own. Is that correct?

Senator GRAMM. No, that is not right.

Mr. MATSUI. Because that is the understanding I have. Now, we will have to look at the actuarial report——

Senator GRAMM. All of this has been scored by the actuaries as working, and let me explain what we do. Currently, the——

Mr. MATSUI. What happens when the surplus is dissipated, the general fund surplus? Because, obviously, you are going into the general fund surplus in order to deal with the unfunded part of this program, particularly if you take the 5 percent and put it in individual investments. I am not suggesting it is being squandered; it is just going someplace else. How do you make up that additional unfunded part of the system?

Senator GRAMM. Well, there isn't an additional unfunded part of the system. If you take the entire $1.780 billion that currently is being projected in our budget and you make these investments so

that by the end of that period 10 percent of all Social Security benefits for people retiring in that year are being funded by the investments they made and 20 years later that is grown to 50 percent. What we are currently showing is this huge deficit in Social Security we are able over time to turn around, and I think the point I am making, which is a fairly substantial point, and that is if you are willing to take now the surplus that belongs to Social Security and invest it in Social Security, we can make the system permanently solvent.

Mr. MATSUI. Well, I still don't follow. We were told by Secretary Rubin a few months ago that there is an $8.5 trillion unfunded part of the Social Security system, because it is a PAY–GO system rather than a funded——

Senator GRAMM. I think that is about a correct estimate.

Mr. MATSUI. I believe that, as well. Now, obviously, you don't take the entire $8.5 trillion; it is 5 percent of 12.4 percent. Now, how do you make that up? It is about $3 trillion.

Senator GRAMM. Let me explain. Here is exactly how we make it up. When I make investments during this transition period, those investments belong to me, but in making up for what I would have gotten had I stayed in the old system, in essence, about 80 percent of the benefits of private investment during the transition period go not to the investor but go to fill up the hole in the current system. That is where the money comes from.

So, what are the benefits? The benefit is to my children. They don't cut their papa's Social Security. Two, we don't raise their payroll tax. They are 20 percent better off than they would have been instead of 7 times better off than they would have been, but their grandchildren—my grandchildren, their children, will get the full benefit of the investment system.

Mr. MATSUI. Well, I will have to do a little more review of this, because I still haven't been able to follow how you make this system work.

Senator GRAMM. Well, the way we—let me try it one more time, because it is a very important question. What we do, every dollar that I pay for my Social Security benefits out of my investments, the Social Security system saves 80 cents.

Mr. MATSUI. Well, I am not too sure. Let me look at it. I am sorry, my time has run out. I really want to——

Chairman ARCHER. I am too. The gentleman's probe is a very constructive one, and the Chair, if you can complete it in another minute or two——

Mr. MATSUI. I appreciate that. I think we have probably reached a point where we might not be able to, and I will, perhaps, talk to the Senator. I appreciate this, Mr. Chairman; you were kind to offer me that time.

Chairman ARCHER. OK, Mrs. Johnson.

Mrs. JOHNSON of Connecticut. My questions go to the same issue.

Right now, more money is coming into Social Security than it costs to support current retirees. So, every year, we have a surplus in our FICA tax fund. Now, discounting past surpluses, which are already invested in Treasury bonds, and, as you say, there is sort of nothing there. I mean, if we pay back those bonds, it is from current spending or new tax revenues or surplus revenues. But, each

year, there is this new money that comes in, and so what I hear you saying is that the surplus income the first year of this plan would be part of what would help substitute for the 2 percent that people are diverting.

Senator GRAMM. Yes, what I am saying is, next year, the Social Security surplus is going to be $138 billion. We are projecting——

Mrs. JOHNSON of Connecticut. Now, is that over and above the——

Senator GRAMM. That is over and above the cost of paying benefits.

Mrs. JOHNSON of Connecticut. OK.

Senator GRAMM. Now, a 2 percent investment would cost in that first year—remember, we are on a calendar year and not a fiscal year, so it is only 9 months the first year—would cost $57 billion; a 3 percent investment would cost $85 billion, and if you did the 2 percent kicker for this age between 35 and 55, these are the people that are going to retire right in the middle of the baby boom generation——

Mrs. JOHNSON of Connecticut. So, basically, in the early years, the surplus funds are able to pay for the diversion.

Senator GRAMM. That is right.

Mrs. JOHNSON of Connecticut. Now, at what point are the surplus funds no longer able to pay for the diversion? At what point does the retired population grow to such a point that we can't fund that?

Senator GRAMM. Well, it depends on your level of investment. What I think is interesting about the proposal that I am talking about here today—and I have got it all written out, and you can look at it—but what is interesting about it is by doing the 3 percent for everybody and the 2 percent as long as the money is available with the surplus for these people that are between 35 and 55, we change Social Security so much by the investments paying benefits that Social Security never goes broke.

Mrs. JOHNSON of Connecticut. So, in other words, the amount of money being drawn out for future retirees declines because of the benefits from the investments.

Senator GRAMM. Exactly. And the numbers I used were the first baby boomer—if we could implement the plan I am talking about—the first baby boomer that retired in 2013 would get 10 percent of their benefits from the investments they made—and that is permanent funding—so the government would only have to pay 90 percent of it, but by the time the last baby boomer retires 20 years later, that baby boomer would be getting 50 percent, on average, of their benefits from their investments, so we would only have to be paying half of it out of Social Security. Hence, this projected deficit in Social Security goes away.

Mrs. JOHNSON of Connecticut. That is very helpful. Now, just two questions. Is this voluntary?

Senator GRAMM. Yes. Under this plan, you would have an opportunity to join the new system or not join the new system.

Mrs. JOHNSON of Connecticut. OK. Now, second——

Senator GRAMM. Now, the truth is everybody would join the new system.

Mrs. JOHNSON of Connecticut. Now, do people over 55 have the same options?

Senator GRAMM. Yes. The people over 65 don't.

Mrs. JOHNSON of Connecticut. Don't. And if you join this and your fund creates—I mean, there will come a time when the combination of the old Social Security system and these new funds will create actually a higher benefit.

Senator GRAMM. That is right.

Mrs. JOHNSON of Connecticut. Now, I assume that your plan does not speak to whether that would go to lower taxes or higher benefits, but at some point in the future, we would make that decision or does your plan make that decision?

Senator GRAMM. No, it is made—basically, a 22-year old could expect upon retirement, based on the historic rates of return we have had, about 22 percent more than they would get under the current system, but they are guaranteed never to get less than they get under the current system.

Mrs. JOHNSON of Connecticut. So, under your plan, any increase in benefits provided by the dual system would automatically go to the recipient and the expectation is that the benefits would be higher.

Senator GRAMM. That is right.

Mrs. JOHNSON of Connecticut. Thank you.

Senator GRAMM. But they always have the guarantee of the current system.

Mrs. JOHNSON of Connecticut. So, it is voluntary. They have the guarantee of the current system, but they have the possibility of really higher returns, and we have the possibility of eliminating an extraordinary unfunded liability through something we are capable of currently funding. Thank you very much.

Senator GRAMM. Well, we have the ability to take this $1.78 trillion that we have now—no one disputes that it exists—and turn it into an investment that can solve the Social Security problem. That is a lot of money; it is a tremendous investment, but I think it—the money belongs to Social Security and when you look at the alternatives, it is obviously the thing we should do.

Mrs. JOHNSON of Connecticut. Impressive. Thank you very much, Senator.

Chairman ARCHER. Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Senator, many other countries that have gone to individual accounts have had trouble with fraud and very, very high administrative costs with individual accounts. Do you have any advice of how we could avoid that, if you go to individual accounts to avoid the fraud and the administrative costs?

Senator GRAMM. Yes, it is something that we have looked at very closely, and let me just make two points. First of all, none of the countries that have gone to an investment system, even the ones that I believe have made a mistake by allowing direct selling and other things, would choose to go back. In other words, even with what are being called excessively high loads, as an investment broker would call it, but fees, as we call it, it still turns out to be a remarkable improvement over the current system.

Now, here is how we deal with it. We don't want people going door-to-door or using the telephone trying to sell, so we set a cap on the fee at 30 basis points, so no one can charge higher than that, and we have looked at this; we have talked to TIAA–CREF; we have looked at Thrift Savings Plans—TIAA–CREF is a college teacher retirement. We have looked at a lot of plans, and, basically, what that will do is produce intensive competition, but, basically, competition where during this once a year when you have the chance to change plans, that you will get in the mail your options. Nobody for that fee would be able to hire somebody to come knock on your door. And in Britain, basically what happened is by not setting a cap on the fee, they created the incentive for people to churn people, to get them to move from one plan to another, and I think it was wasteful, and it was unnecessary, and I think we have learned from it, but it is important to remember even with the churning that the average worker in Great Britain is better off, but they could have been much better off had they set a cap on it to try to eliminate direct selling, which is basically what we have done.

Mr. COYNE. Thank you.

Chairman ARCHER. Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman.

Senator Gramm, I want to commend you for coming up with what appears to be a very solid plan for saving and improving Social Security.

I have read the letter from the chief actuary, and I don't find in his letter—perhaps, you can tell me—what rate of participation in the voluntary plan does he assume in making his projection?

Senator GRAMM. He assumes 100 percent. Now, in the early years, it would actually be easier if fewer people participated, but you have got to remember, we guarantee that you can never be worse off than you were under the old plan. We don't take any benefit away, and so it is all upside, no downside. So, the assumption is that within 2 years, that for all practical purposes, everybody will opt-in to the new system.

Now, what will happen is that you don't go into the new system unless you choose a money manager to manage your funds from those that are licensed based on meeting the highest standards. So, what will happen is you will get one person who doesn't know how to choose; they will go home to visit their mamma; their brother is there who is a know-it-all, and he will say, "Well, how are you doing on your investments?" And he will get his thing from Prudential and show how he is doing, and you will say "Well, I haven't decided who I am going to go with yet," and you won't say so at the time, but you will go back home and sign up with Prudential. But over a 2-year period, it is our assumption that everybody will opt-in to the new system.

Mr. MCCRERY. Well, I think that is a flaw in your plan, frankly. I think that is a very optimistic assumption, but——

Senator GRAMM. Well, they don't stand to lose anything. They have got the same government guaranteeing the benefit, so we assume over time that they will make that option. If they don't, it is much cheaper on the front end; it doesn't save quite as much on the back end.

Mr. McCRERY. I know it is not a direct analogy but a 401(k) plan is very attractive too, and we have a miserably low rate of participation in 401(k) plans. It is a lot better now than it was 5 years ago, but it is taking a long time for it to sink in to many, many workers in this country that it is to their advantage to invest in a 401(k). Even with their employer matching, we still have a low rate of participation.

Senator GRAMM. Well, but, remember, imagine if you had a mandatory government 401(k) where the government invested it in government bonds and you had the option to opt-out of it. That is the comparable comparison.

Mr. McCRERY. If everyone were educated in the facts surrounding that, I agree with you, but that is not the case in our society today, and I just think that is an overly optimistic assumption. So, I would like to see, Mr. Chairman, the actuaries give us some projections based on lower rates of participation, so we could get——

Senator GRAMM. They could certainly do that.

Mr. McCRERY. Yes. Your proposal includes a recapture of corporate tax, and I have to admit I have not read your plan, and so I don't understand that. Can you explain that?

Senator GRAMM. OK, let me explain it. For the last 75 years in America, the rate of return on 60 percent stocks and 40 percent bonds has been 8.5 percent, but no investor ever saw that rate of return, because the Federal Government took 2 percentage points off the top in corporate income taxes; State and local government took 1 percentage point in State corporate income taxes and State and local property taxes. So, that the rate of return we are using here is an after tax rate return of 5.5 percent, and then we take off the load reducing that down—that is the management fee—reducing that down further. All we are doing here is simply setting up a procedure whereby at the end of the tax year when all corporate incomes taxes have been collected, that we have the Treasury remit to the Social Security system the amount of taxes they have collected on the investments that have been made in Social Security investments. So, this is not a new tax; it is simply revenues that the government is getting because of these investments being made. No one could ever earn 5.5 percent if 8.5 percent weren't being paid pretaxes. So, it is confusing, but that is where it comes from.

Mr. McCRERY. Well, is that then deposited into the Social Security Trust Fund?

Senator GRAMM. That goes to the Social Security system to help pay for benefits.

Mr. McCRERY. Yes, which is then used to either pay benefits or finance the accounts.

Senator GRAMM. Well, no, it doesn't go—it goes to pay benefits. It goes to pay—we raise the minimum benefit in the plan, and it is one of the things that funds it. We would like to make these investments tax-free, because there is no reason that we should be taxing Social Security investments, but we don't know how to do that, so the best we could come up with that would end up being scored is to try to recapture it based on an estimate when you have already collected the taxes; you know what the total level of invest-

ment in the economy was; you know how much Social Security is invested, and you just use a simple formula assuming a certain amount of leakage and a certain amount being invested abroad, and that has to rise over time, because if you actually make these investments for the first 30 years, they don't make that much difference, but after that, they get big enough that they start meaning that either the rate of return is going to decline or you are going to invest more abroad or both, and we assume both those things.

Mr. McCRERY. Have you, yet, had your plan scored with respect to the unified—the effect on the unified budget surplus?

Senator GRAMM. The effect on what?

Mr. McCRERY. The unified budget surplus.

Senator GRAMM. Yes, it has been scored based on the unified budget surplus, yes.

Mr. McCRERY. No, I mean, do you have a table showing us the outyear effects on the unified budget surplus?

Senator GRAMM. The actuaries at Social Security have shown the Social Security surplus, the non-Social Security surplus, so you can calculate the two. I can get that to you.

Mr. McCRERY. OK, thank you.

Chairman ARCHER. Mr. Doggett.

Mr. DOGGETT. Thank you. I wanted to focus in on the disability aspect of your plan. I noticed that you have people going into a new cooperative disability insurance system. How will that work?

Senator GRAMM. Well, I don't do it in the first bill, Lloyd. What I do is simply set aside 2 percentage points for disability. So, we would continue to fund the current system under the bill that I have introduced. What I would like to do over time is to set up a self-contained disability program that would be funded the way we would fund Social Security, and it would basically be you would set up a board that would have the Secretary of Labor, the Secretary of the Treasury; you would have three outside members, one of whom would be chairman, and you have them enter into contracts with private companies to do it. You wouldn't have to do it; it is not essential to plan, but part of our problem in disability, which is an excruciating painful problem, is that while mortality and morbidity rates have fallen, while on-the-job injuries have fallen, disability rates have skyrocketed.

Mr. DOGGETT. So, your goal is to have a disability insurance plan that is basically managed by private companies on contract?

Senator GRAMM. Well, it would be managed by the government, but we would, in essence, buy private insurance that the government would guarantee. In the long run, I would like to do that, and the reason is to get the definition of disability out of the hands of politicians, because what we have done on a bipartisan basis, I might add, for the last 30 years, is we have constantly lowered the threshold for disability, and so while all outward measures of disability in the economy have gone down, our number of people who are, quote, "disabled" has gone through the ceiling, and in Europe, 60 percent of people over 60 are disabled.

Mr. DOGGETT. So, the goal would be to let the private companies define disability——

Senator GRAMM. Well, the goal would be to define it once and to quit changing it, so people would know what they are buying into.

It is not essential to the plan. The way the plan is written you still have got 2 percentage points going to pay for disability. You could fund the current disability program.

Mr. DOGGETT. As you are well aware, I think you got some attention in today's National Journal of Congress Daily on it. There is a plan up this year to try to reduce those Social Security disability roles by encouraging people to return to work so they can maintain their health insurance, and you are credited with stopping that plan in the Senate. As I understand, you support the plan; it is the way it is funded that you question?

Senator GRAMM. Yes, basically, we have a proposal in the Senate that would allow people to go back to work and keep Medicare and Medicaid. I think it is a well-drafted proposal. We have made a lot of changes in it. The problem is rather than coming up with a savings to pay for it, we have, in essence, raised taxes to pay for it, and I am afraid in the midst of busting the budget caps on discretionary spending, if we set the precedent for raising taxes to expand a benefit, any benefit, create a new entitlement program, any entitlement program, that we are just opening the flood gates. So, what we are trying to do in the Finance Committee is to come up with a savings to pay for it, and I think we will do it. I think it will become law.

Mr. DOGGETT. I hope you are able to accomplish that. Thank you.

Senator GRAMM. Thank you, Lloyd.

Chairman ARCHER. Senator, we do have a couple of other questioners, but I want to alert the Members of the Committee that it is the Chair's intention to not break for lunch, and any Members who wish to go out and grab a sandwich on their own should do so and then return as quickly as they want to participate in the hearings.

Mr. Herger.

Mr. HERGER. Thank you, Mr. Chairman.

Senator, I want to thank you. This is very exciting. We have, for so many years and certainly months, recently, all we hear about is how Social Security is going bankrupt; how we are not going to have enough money; how we are basically mortgaging the lives of our children and grandchildren. So, to hear something exciting, particularly this concept of compound interest and, as you mentioned, Einstein saying the most powerful concept in your graph, is really very intriguing.

I would like to understand a bit, if I could, maybe talk a little bit about the individual accounts and how they relate with some of the other plans, and I would like to, if I could, maybe ask several questions. I think you have already mentioned this, but with comparison with others, is your account voluntary or mandatory? I believe you mentioned it is voluntary.

Senator GRAMM. Yes. Let me just do the accounts, and then—I will forget them by the time you get to the bottom of your list.

Mr. HERGER. Well, I will ask them one at a time.

Senator GRAMM. How basically it works is, is that we allow people to opt-in to the system. Companies that want to manage funds submit their credentials to a new Social Security Investment Board that would be made up of the Chairman of the Federal Reserve Bank, the Secretary of the Treasury, the head of the SEC, and two

outside members that are financial experts, one of whom would be chairman. They would be appointed—the outside members would be appointed by the President and confirmed by the Senate. They will look at all these groups that want to manage Social Security money, and based on the highest standards of safety and soundness, they will certify or qualify plans. Then any worker can choose from among the qualified plans to manage their money. Once they have chosen a plan, they don't exercise any decisionmaking over the investment, itself. By choosing the plan, they, in essence, choose the investment strategy.

Now, we also set, by law, for safety and soundness, for the first 3 years, no more than 60 percent in stock; no more than 3 percent in any one stock, but this would be chosen by the money manager. After 3 years, we let the Board, subject to safety and soundness, set these parameters for workers. That is basically how it would work.

The second question was what? I knew I would forget, and I did.

Mr. HERGER. Well, how would these accounts be used to support Social Security benefits and retirement?

Senator GRAMM. OK, how they would be used is, when you retire, you take your safe accounts, as we call them, and you convert those into a variable annuity, and the variable annuity pays you an amount per month, and then if that is less than you would have gotten under Social Security, the Social Security Administration makes up the difference. If it is more than you would have gotten under Social Security, it all belongs to you, and during the transition, it will be less, and we structure it so during the transition you will always get to keep 20 percent of the investment value above the amount that Social Security would have replaced. So, during the transition, you always are at least 20 percent better off based on the investment you made. Once we are fully into the system, the investments belong to you.

Mr. HERGER. They belong to you. Would there be something you could leave to your heirs, say, if you died somewhere along the line?

Senator GRAMM. Yes, if you die before you convert to the variable annuity—because, remember, an annuity is a combination of insurance and investment, and part of what the company is betting on—you are betting you are going to live; they are betting you are not going to live, in essence, and some people are going to live longer than they expect; some, a shorter period of time—but before you retire, if you die, your entire investment goes to your family.

Mr. HERGER. Somewhat of a built-in life insurance policy, if you will. And did you also mention that—let us say we do have a downturn in the economy, which we have had; you have mentioned we have went through a depression even though we have averaged 8.5 percent, there are those downtimes—you mentioned that there would be minimum amount that would be guaranteed to these people——

Senator GRAMM. We guarantee the amount that Social Security would have paid anyway. Let me give you a numerical example. I think that we are assuming by 2020 that we would have $7 trillion invested in these accounts. But let us say that we had the equivalent of the Great Depression, and we had only $5 trillion in these

accounts. Are we better off with $5 trillion or zero? Under the current system, we got nothing. Under this system, you would have $5 trillion under the worst of circumstances; $7 trillion under what we expect to be the norm; maybe $9 trillion under the best of circumstances, but the point is you would have had nothing under the old system, and you still got $5 trillion, so the government would have to make up the difference, but they would have had to pay the entire benefit under the old system.

Mr. HERGER. But, again—I understand, but, again, just to make it clearer, those who are retiring are, at minimum, guaranteed what they would have been receiving anyway under Social Security. Is that not——

Senator GRAMM. Yes, no one would ever get less under this plan than they would have gotten under the old system.

Mr. HERGER. So, it would almost seem—anyway, it sounds very positive. I thank you very much, Senator.

Senator GRAMM. Thank you.

Chairman ARCHER. Mr. Foley.

Mr. FOLEY. Thank you very much, and, Senator, thank you for joining us today and for any Member willing to talk about Social Security, I applaud them.

The concern I get, though, when we talk about these plans, there is a lot of conversation about guarantees. We will guarantee you at least current recipients will have the same as they would have had they stayed in the system. There doesn't seem to be an investment on Earth, though, that I can find that makes that promise, because everything has speculative risk. If you bought Amazon.com at $3, today, you are thrilled. If you bought it at $247, you may not be as happy today, and you are going to have those ups and downs. What is the mechanism by which we ensure these accounts in the event you have a hedge fund that collapses where you had significant investment? I know of stories of friends who had all their eggs in one basket, ESOP plans where they bought the company stock as their collateral or their equity, and the company went out of business and left them stranded. How do we, as a U.S. Government, ensure these projections go forward; that we have the kind of returns you anticipate, but also backdrop that with this ironclad guarantee that you will never get less than what you were promised today? It seems to be——

Senator GRAMM. Let me explain how it can work. First of all, you are guaranteed today based on no assets whatsoever. You have got an ironclad guarantee that we are going to pay benefits in the future, and we have no investments; we are getting no rate of return; we are just simply committing that some future generation is going to pay that money. So, to the extent that we substitute real wealth—we really have a system today based on debt, the debt of future taxpayers. We are beginning the process here in a 39-year transition to substitute for that a system of wealth. But we maintain the guarantee which is that if something does go wrong you are no worse off than you would have been under the old system. The government is no worse off financially than it would have been under the old system. In fact, it is always better off, because you have got some investments.

Also, the examples you used were examples where people concentrate their investment. We are not going to let people invest this money with their brother-in-law, because we are guaranteeing the result. We are going to have an investment board that is going to set parameters, and it is going to oversee just as the SEC does the regular market, but with much higher standards, the investments that are made, and if a company begins to perform poorly, the board has the ability to force them to change policies or to come in and shut them down—they never take ownership of the stocks and bonds—and transfer those accounts to another firm. In fact, in Australia and in Chile, that has happened on several occasions, and nobody lost any money in the process.

But the reason you can guarantee it is that we are guaranteeing it now with no assets with an ironclad guarantee to the extent that government guarantees are ironclad. We are going to be supplementing, over time, more and more wealth to take the place of debt, so it is much easier for us to guarantee what I am guaranteeing in this plan as compared to what we are guaranteeing under current law. That is the point.

Mr. FOLEY. At what age does this plan actually take effect for a recipient? Is there a guarantee today, currently, that they all stay in the system?

Senator GRAMM. Yes, you would begin to exercise the choice on January 1, 2000, and it is a good point I think to end on. Every day we wait, we are guaranteeing that we are going to cut benefits and we are going to raise taxes. If we don't get into this—no matter whether you choose Chairman Archer's plan or my plan or whoever's plan, time is critical for this money to grow, and if we don't get into it in the next couple of years, there is no way that we can deal with this problem that will not entail tax increases and benefit cuts. So, timing is critically important, and when the President, in essence, did this cop-out with the plan he came forward with after having spent 2 years first saying save Social Security now or first and then save Social Security now, it really was a major step toward tax increases and benefit cuts. You can't wait 4 or 5 years and make this work, anybody's plan work. Now, you will be better off doing it 5 years from now than never doing it or better off doing it 5 rather than 10, but if you want to avoid cutting benefits or raising taxes, you have got to do it next year.

Mr. FOLEY. Thank you, Senator.

Chairman ARCHER. Senator, thank you for a very cogent presentation. We appreciate your coming and appearing before us.

Senator Moynihan, my apologies for keeping you waiting, and thank you for your patience and your perseverance, and I would like to add an even additional amount to that in saying that you have been a great public servant over the years; made an enormous contribution to your country. You have asserted an independence in your beliefs which I think is an enormous credit, and I personally am pleased to count you as a friend, and I have enjoyed working with you over the years, and I welcome you to the Ways and Means Committee.

The rule that we are operating under is that we are asking each witness to limit their testimony to 10 minutes, and the entire writ-

ten testimony, without objection, will be inserted in the record, and welcome to the Committee. You may proceed.

STATEMENT OF HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM THE STATE OF NEW YORK

Senator MOYNIHAN. Thank you, Mr. Chairman. I could not be more grateful for your gracious remarks. I hope you understand how much I reciprocate them. We have been at this together a long while and have seen some successes, and I think we may yet, too.

A number of my colleagues on the Senate side will be speaking later, as has my friend, Senator Gramm, about a larger use of Social Security bringing into the idea of accumulating wealth, a matter that Senator Kerrey very much feels strongly about, about providing annuities or providing an estate for people who work all their lives; profoundly important ideas, new and appropriate I think to the new century. I am going to speak to a more traditional Social Security arrangement which simply ensures that the existing benefits are paid for the next 75 years.

Sir, I have four points and four points only. On the more than one occasion when a senior member of the President's staff has said we are going to have to get to work on Social Security, I have taken the liberty of producing a 500-page notebook, which I sent to the White House, with 1 page of text and these four points. At this moment, I should say to Mr. Herger—who has had to leave for the moment—the feeling that Social Security is going bankrupt, no, sir. Social Security is not going bankrupt. In the next 10 years, we have a surplus in Social Security of more than $1.7 trillion. Now, there will come a time, but let us be clear about that dimension.

The reason we have that surplus goes back to the legislation we adopted in 1977, a long time ago. If I had said 1777, it would not have been much difference in the perspective of Senator Roth and I who are the only two Members of the Conference Committee still in the Senate. I don't know if there are any still from the House. But, at that point, we took Social Security from the pay-as-you-go basis that was established in 1935 in the midst of the Depression to a partially funded basis. That profound change attracted almost no attention. I was a member of the Conference, a very serious member. It was my first conference ever. I had no idea we had done that. If the New York Times reporting on the event knew it, they chose not to mention it. You will find a few lines about it in the Conference Committee report, not many. It was basically a decision by the Social Security professionals. And that continues to be.

We have had that surplus all through the eighties and much of the nineties. We are now thinking about putting a lockbox that the House has just proposed—and a very sensible one, if I may say, particularly if an escape for recession is added—but Social Security has a surplus.

Chairman ARCHER. Senator, I apologize, but I have got to go vote, and Congressman Shaw will preside until I can return.

Senator MOYNIHAN. What a pleasure that will be, sir. You do your duty.

Mr. SHAW [presiding]. Yes, sir. Please proceed.

Senator MOYNIHAN. Thank you, Mr. Chairman.

The four points, which I mentioned, do provide a Social Security solvency for 75 years, and this is the situation. As presently constructed, we have a 75-year deficit of 2.07. These four points would reduce the deficit by about 2.2 so that in fact you would have a small surplus over 75 years. The first point is to reduce the cost of living adjustment by 1 percentage point. This has aroused a lot of opposition, but I should say to you, sir, it is a bit presumptuous, but I don't know of a prestigious economist in the Nation who does not think, believe, can demonstrate that the cost of living adjustment overstates inflation. The U.S. Department of Labor, Bureau of Labor Statistics says so. They have a little pamphlet they put out called *Understanding the Consumer Price Index*, and there is a number of questions, and question number three: Is the CPI, Consumer Price Index, a cost of living index? And they say, "No, although it frequently and mistakenly is called a cost of living index," and they go on to explain the number of reasons for this, and if you want to go into them, I can do that for you.

The commission headed by Professor Boskin at Stanford, which was appointed jointly by Senator Packwood and I about 4 years ago addressed this question, and very seriously people have been working with it for 30 years, said that the CPI overstates inflation by something of between 0.8 and 1.6 percent, and in that range you will find most such estimates. Alice Rivlin, when she was Director of the Office of Management and Budget, gave about the same estimate in an internal document that made its way into the public domain. Reduce cost of living adjustments. Still use the CPI as we now do, but just take 1.0 percent off that number.

Second, tax Social Security benefits in the same way as private pensions, which is to say any part of the benefit that you haven't previously paid taxes on, you now pay taxes on. It is just treating it as a pension, which it is.

Third, extend coverage to all newly hired State and local government employees. This is a real anachronism. Back in 1935 when for the longest while it wasn't clear that Social Security was constitutional, the Federal Government could not tax a State government or a subdivision of a State government. So, State and local employees are not required to be covered under the statute. Three-quarters have opted to do so, because it makes sense, but there are five million persons who don't pay now. Most of them get Social Security by working on the side and so forth. Just make it a universal payment.

And, fourth, a technical point, Mr. Chairman, increase the computation period from 35 to 38 years. That just reflects the fact that since people live longer, their working lives are longer.

Do those four things, and take up the subject 75 years from now.

Mr. SHAW. Well, you have another minute, but I think it shows the uniqueness of Senator Moynihan in being able to stop a minute short, as a Senator, in the amount of time allotted you.

I want to personally congratulate you on your long distinguished career. We have worked together on welfare reform——

Senator MOYNIHAN. We have, sir.

Mr. SHAW [continuing]. And I know that you sounded the alarm bell on that back there in the Nixon administration, and you were so right.

Senator MOYNIHAN. Johnson, sir.

Mr. SHAW. Johnson? Well, you came up with some figures during the Nixon administration also with regard to out-of-wedlock births and some of the things that were happening, but you certainly are putting yourself in the forefront of making some very tough stands with regard to Social Security, and I want to congratulate you for your involvement.

I would also tell the Members that I know you have another commitment, and I will have to shorten the time for questioning.

Senator MOYNIHAN. Well, I am at your disposal, but you have so many other witnesses.

Mr. SHAW. OK, thank you.

Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Senator, thank you for your testimony. I have always been wondering why we have this cap, $68,000, in paying into Social Security. People earn up to $68,000 and then they are taxed for it, and it is matched by the employer. Is there any good reason why that should continue to stay on in a time when we are looking to resolve the problem with Social Security?

Senator MOYNIHAN. If you look to the formulas by which we pay out benefits eventually, there is a reason for that, sir. You could argue to expand it. We do extend it from time to time. May I say that is an issue I would wish we would be careful about, because we want Social Security to seem an equitable return to everyone, and if you get to the point where people in the high-income brackets are paying so much more than they are ever going to get back, you start losing the universal quality which has produced the extraordinary support for this program, although it is a fact and it bedevils, which is that a majority of nonretired adults in this country do not think they will get Social Security.

Mr. COYNE. Thank you.

Senator MOYNIHAN. Thank you, sir.

Mr. SHAW. Thank you.

Mr. Neal.

Mr. NEAL. Thank you, Mr. Chairman.

Senator Moynihan, welcome. It is nice to have you here as always. I tell everybody here that you are as good a dinner companion as you are a witness.

Let me ask you a question. We have had testimony, substantial testimony, all morning about actuarial tables, about projected growth rates; and about 2 percent here and 4 percent there. But based upon your long and distinguished career here and based on the universal acclaim that Social Security has won, could you speak for a moment of the importance of community in Social Security; how we are all linked together by this New Deal Program?

Senator MOYNIHAN. Well, exactly so, and that was my response to Mr. Coyne, that we understand that this is an insurance program into which everyone pays and everyone gets a return, and there is no large difference in that return. We do tilt the benefits to low-income persons, and that has been from the beginning, and we understand why, but in the main, it is a shared enterprise. I think we did get a little too confident about it. And the administrators for a long period there had—they knew the system was in good

shape, and that was enough for them to know, and it took me, oh, 15 years to get the Social Security Administration to start sending out on an annual basis the personal earnings and benefit statement so that from the time you are 18 and have your first job, you know that Social Security knows your name, your number, and is recording your contributions. They just didn't want to do that, and it wasn't necessary, they thought. The next thing, they looked up, and there was this lack of confidence in the system.

We also had to restore the Social Security Administration to its independent status. It began as such, then got jumbled up in New Deal agencies and then the Hoover Commission, and the next thing you know in the 1994 Congressional Directory, there were more than 200 names between the Secretary of Health and Human Services and the Commissioner of Social Security; it was way down there. We passed a bill which recreated an independent agency with a fixed 6-year term for the Commissioner.

But, yes, I think the more we let people know, "We know you are there; your money is safe; you are going to get it," that sense of community will return. It has in fact eroded somewhat.

Mr. NEAL. Thank you. And based upon your long career, would you deem Social Security to be the great legislative accomplishment of this century?

Senator MOYNIHAN. Yes, yes. I mean, it took life from being perilous and solitary, nasty, brutish, and short for all too many people into making us a community in which we could live together, live longer, be better—I think we are better. I knew Francis Perkins, and let me tell you, that was a great woman.

Mr. NEAL. Thank you, and Hobbs would like your quote. Thank you.

Mr. SHAW. I would like to add to that on what you just said, Senator, that it is not only one of the great legislative accomplishments, it is also the greatest antipoverty program ever devised by Congress, and it certainly must be preserved.

Senator MOYNIHAN. You get money, you get income, if you work.

Mr. SHAW. All for the right reasons; yes, sir.

One further question that I have and then I will yield to Mr. Rangel. In your plan, you have a component, a voluntary component, as to individual savings accounts. Do you think that this would be possible to pass the House and the Senate, and, if so, do you think it is something that the President could sign?

Senator MOYNIHAN. Yes, sir. I would have to say that if we take that 2 percentage points, above what we need for pay-as-you-go and turn that into a personal savings account system, rather like the Federal Thrift Savings Plan, it would be a logical extension of the big social programs of the 20th century. First of all, unemployment insurance. That was the great trauma of industrialism. You are suddenly out of work and you have no money. It was a new thing, and nobody could explain it, because, you know, you are never out of work on the farm; you may be half starved, but you are not out of work. And this came along—insure unemployment. Then provide for retirement benefits for people who no longer, again, are living on the farm where you can have something. Then health care and now, finally, to a lifetime savings. It is a paradigm that you can hardly resist in its logic.

Yes, you could do this. I do not think it has to be complicated. I think the more complicated, the worse. I think that just going to the Federal Thrift Savings Plan with individual accounts—if I could interrupt myself here for one moment, there is talk, and it comes from downtown, of taking some of this money that we are going to save and put aside and investing it in the stock market. Sir, don't do that. I mean, it just—don't put that temptation in front of us. It could be ruinous, and let us do this in a way that doesn't end up manipulating the economy which is what would happen.

Mr. SHAW. Mr. Rangel.

Mr. RANGEL. Thank you. Senator, I know that you have many days and months before your term expires and many legislative accomplishments yet to achieve, but I just wanted to take this moment as the Dean of the New York State delegation and a longtime Member of this House to sincerely thank you for making us so proud to be Members of Congress, so proud to come from the great State of New York, and so proud to work with you over the years. I do hope that your contribution here today will allow all of us to have the political courage to come together in a bipartisan way in working with the White House, not for political gain, but to see how we all collectively can say we met the challenge and that we have done the right thing. You have been a great friend and an even greater legislator, and I just wanted to take this moment to say thank you.

Senator MOYNIHAN. Well, thank you, my dear friend and my leader of the delegation. Might I just say that in 1983—well, earlier than that, 1981, President Reagan having been told there was a crisis in Social Security, and indeed there was a short-term crisis, in the late seventies, for the first time in the history of our statistics, prices increased faster than wages, and the trust fund was getting very low, appointed the National Commission on Social Security Reform. We worked in public for 2 years, and we ended up failed utterly. Then Senator Dole asked me if we could talk a bit—this was after we were finished and failed. From January 3, the day we swore in the new Congress, he brought over our very good friend from the House side——

Mr. RANGEL. Barber Conable?

Senator MOYNIHAN. Sir? Yes, yes. And a day later, we were in Secretary Baker's basement, sort of rec room, and 2 days later, we were in Blair House which is being fixed up, and in I think a total of 12 days, from beginning to end, we worked this all out; President Reagan watching it very carefully and agreeing. When you are working together, this is not an impossible job. Revenues are much up right now, because unemployment is so low. But I would say this to you, sir, that let us do it before we get to a crisis. It is a lot easier.

Mr. RANGEL. Thank you, sir.

Mr. SHAW. Are any other Members seeking recognition? Yes, sir. The gentleman from Ohio.

Mr. PORTMAN. Senator, I echo the comments that were made by others to thank you for your service and your courage to step out a couple of years ago when others weren't talking about it to dis-

cuss ways in which we could begin to adjust Social Security so that we wouldn't be acting in a crisis situation but rather be prepared.

I like a number of the provisions that are in the Moynihan-Kerrey proposal. The one I don't like is that newly hired State and local workers would be included, and we could talk about that, but I think that the State program in Ohio and other States are probably programs that we should begin to look at emulating in that they are prefunded and working and not in an insolvent position.

But if I could ask you about KidSave. This is an intriguing idea to me, and I wondered how it was integrated into the Social Security Program or is it along the lines of the Thrift Savings Plan that, in essence, is outside of Social Security but would supplement Social Security through private savings after retirement?

Senator MOYNIHAN. You are entirely right, Mr. Portman. This has to do with the tax system of the Internal Revenue Code and the use of general revenues. It is Senator Kerrey's idea, and it is a wonderful one, but it is not a Social Security Program.

Mr. PORTMAN. OK. He has now arrived behind you, so you have to be careful what you say.

Senator MOYNIHAN. Oh, it is a wonderful——

Mr. PORTMAN. Wonderful is a good adjective.

Senator MOYNIHAN. Did I say that with enough emphasis.

Mr. PORTMAN. Again, thank you for taking the time to be here today and for your pioneering work on this issue.

Senator MOYNIHAN. Thank you, sir.

Mr. SHAW. Mr. English. No questions. Any other Members seek recognition? If not, Senator Moynihan, it is a pleasure as always to have you and see you over on the other side of the House.

Senator MOYNIHAN. Honor to appear before you, Mr. Chairman, Mr. Rangel, Mr. Houghton——

Mr. SHAW. I am delighted, too, to see that you got over your surgery satisfactorily. That is high-risk surgery, I can tell you that.

Our next panel, I see Senator Kerrey and Senator Gregg are here. If they would sit at the witness table, they will be accompanied by Senator Grassley and Senator Breaux when they come in.

Senator Gregg, you are up to bat. Nice to see you back.

STATEMENT OF HON. JUDD GREGG, A U.S. SENATOR FROM THE STATE OF NEW HAMPSHIRE

Senator GREGG. It is great to be here. It is a wonderful Committee, and I had the great privilege of serving here.

Mr. SHAW. Your microphone is——

Senator GREGG. I had the great privilege of serving on this Committee for a number of years, and it was a wonderful experience.

Senator Kerrey and myself, Senator Breaux, and Senator Grassley are here to talk a little bit about the plan that we have proposed and any other Social Security issues which are floating around, and we certainly appreciate this Committee's patience, because you have been taking testimony for a long time, and you are probably Social Security's out.

Let me highlight some of the ideas within our plan. First, and I think very, very significantly, this is a bipartisan proposal. It is a proposal that was pulled together across the aisles in a construc-

tive way, and it took a lot of negotiation to reach agreement, but we did reach agreement. And it is supported by a pretty good spectrum of Members from both sides of the aisle. We are the primary sponsors here today, but we have a fair number of cosponsors on both sides who have joined us.

Second, it is a plan which accomplishes what must be the true goal of Social Security reform, which is that it makes the Social Security system solvent for the next 100 years, and that is a scoring that was done by the Social Security actuaries, and that is a threshold issue in my opinion.

Third, it addresses what I think is a critical issue, which is that we not end up creating a huge tax burden on the general accounts of this government as we try to address the Social Security system problems in the outyears. As we all know, in the transition period, from about the year 2015 through about the year 2045, we are going to have a tremendous amount of pressure to figure out how to get over those years as the huge baby boom generation retires and as the defined benefit exists and must be paid for, and the question is, is that defined benefit going to be paid for out of prefunded liabilities, which is a prefunded activity, which is I think the best approach? Is it going to be paid for out of new taxes on wage earners? Is it going to be paid for out of raising the Social Security tax? Is it going to be paid for out of benefit cuts? In our proposal, we do not raise taxes. We think that that is a critical element.

Third—or, fourth, our proposal addresses what I think is very important also which is that we try to mute the intergenerational disparities within the Social Security system as we move into the next generation receiving benefits from the Social Security system. As we all know, a young worker today, coming into the labor force, is going to get a very poor return on their Social Security taxes. We attempt to address that issue. We address it through making the system progressive, more progressive than it presently is, and by making the system spousal-friendly, so that especially women who are today at a disadvantage under the system are addressed more fairly, and Senator Grassley will, I think, talk about that.

Fifth, we do have as our core element in our proposal the idea which has been discussed at length this morning of giving people ownership over part of their Social Security taxes through a personal savings account. Our personal savings accounts vary in size depending on a person's income, with low-income people having the ability to get a personal savings account of up to 4 percent and high-income people having personal savings accounts of 2 percent, and it is done by cutting the payroll tax and refunding that and allowing people to invest that personal savings account under a system which is designed and based on the Thrift Savings Plan which is presently—many of us in the Congress take part in, so you are familiar with it. So, we do have that element of trying to prefund the liability of the system by giving people ownership over an asset which will grow.

Also, I think it should be noted that we do not have that asset forfeited when people get to obtain their retirement benefit. That asset is owned or the savings account is owned. If a person dies before they reach retirement, their estate receives that asset that has

been built up in the savings account, and when a person retires, we do require that for some, a portion of the benefit be annuitized, but we also reward them. Whatever they are able to earn over the basic rate of return which would occur on bonds is theirs, and there is no clawback of those funds, and they do not have to offset them against their benefit, which is, we think, a very—creates a great deal of incentive for people to stay in the system and to feel that the system is going to be there and benefit them when they retire.

I want to stress again that our system is structured to be more progressive. We have a higher minimum benefit under our proposal than under the present Social Security system. That is without taking into consideration the personal savings account, and, of course, as I mentioned, the personal savings account is the asset of the retiree, and, as a result, especially low-income situations, it is likely that that asset is going to accrue at a rate that is fairly significant as we allow up to a 4 percent contribution to it.

I think that touches on the main themes of our proposal. Let me talk just quickly about—and, as I mentioned, our proposal works. It has been scored; it is substantive; it is a combination of a lot of different ideas that are out there. Senator Kerrey had some ideas; Senator Breaux and I had some ideas; Congressmen Stenholm and Kolbe have ideas. We have taken a lot of these ideas, and we have merged them. Senator Grassley has got some strong ideas in the area of widows' benefits. So, we have taken them all, and we have merged them, and we have produced this package, which we think is a very strong proposal and which, if it were adopted today, it would correct the problems of the system and create a system where we would have beneficiaries who, not only today but for the foreseeable future, the next 100 years, would be able to be assured of a good Social Security benefit. I would note that our system does not impact in any way people who are retired today or are about to retire, so we don't impact their benefits.

I wanted to talk just quickly here, though, about a concept which I think is absolutely critical to understanding this problem, and I know many of you are familiar with it, but I just want to stress it again if for nothing else than the presses, and that is this whole issue of the fact that as we move into the outyears and the postwar baby boom generation retires and there are so many retirees taking from the system, that under a system that is a defined benefit system which says that those retirees are going to get a certain benefit, the trust fund is irrelevant unless the trust fund is owned and prefunded by the retirees. If the trust fund is filled with notes, obligations of the Federal Government, then it simply becomes a tax burden on the next generation to pay the defined benefit. The notes are essentially irrelevant. If the defined benefit is there, you are going to have to raise taxes to pay for them. The President's proposal, for example, is simply a massive shift of the obligations of the trust fund to the general funds of the Federal Government and, therefore, to the taxpayers. And what I think we have to look at very aggressively as we move forward in Social Security reform is not seeing—is looking at the overall picture and not missing the fact that the total tax burden, not just the Social Security, but the total tax burden to support the system is what must be addressed, and if you are going to have a dramatic increase in the total tax

burden to address the system because you have got to use huge amounts of general funds to support the system, then you really haven't done anything other than to shift the burden of paying for the system to the younger generation, and the younger generation is already getting a very bad deal under the present Social Security system, as we all know. And, so to just increase the negative effect of that deal by simply filling the trust fund up with notes or some other obligation which has no tangential asset behind it, which is owned by the retiree, is inevitably going to make the new retirees' return even worse, and, therefore, make the system less supportable and less defensible to people who are in their twenties and thirties and are coming into the system.

And I do think that as we move forward and discuss all these different proposals that have been put before you, that you need to look very hard at what is the overall tax liability that is being generated here, and are we really doing anything for the younger generation if we dramatically increase the general fund obligation to support the Social Security system?

Thank you, Mr. Chairman. I appreciate your attention.

[The prepared statement follows:]

Statement of Hon. Judd Gregg, a U.S. Senator from the State of New Hampshire

Thank you, Mr. Chairman, for this opportunity to testify before your Committee. I want to compliment you for your leadership on this important issue—not only for holding these hearings, but also for offering a reform proposal of your own.

The proposal that I will discuss was negotiated over several months between a bipartisan group of committed reformers in the Senate. It already has more cosponsors than any other competing proposal. Those cosponsors include myself, Senator Bob Kerrey, Senator John Breaux, Senator Chuck Grassley, Senator Fred Thompson, Senator Chuck Robb, and Senator Craig Thomas.

What I want to do in my remarks is to describe what our proposal would achieve, and then to provide some details as to how it achieves these goals. It would:

—*Make Social Security solvent*. Not simply for 75 years, but perpetually, as far as the Trustees can estimate. Our proposal would leave the system on a permanently sustainable path.

—*Increase Social Security benefits* beyond what the current system can fund. I will follow up with some details as to why and how.

—*It would drastically reduce taxes* below current-law levels. Again, I will provide details as to why and how it does this.

—*It will make the system far less costly* than current law, and also less costly than competing reform proposals.

—*It will not touch the benefits of current retirees.*

—*It will strengthen the "safety net" against poverty* and provide additional protections for the disabled, for widows, and for other vulnerable sectors of the population.

—*It will vastly reduce the federal government's unfunded liabilities.*

—*It would use the best ideas provided by reformers across the political spectrum*, and thus offers a practical opportunity for a larger bipartisan agreement.

—It will improve the system in many respects. *It will provide for fairer treatment* across generations, across demographic groups. *It would improve the work incentives* of the current system.

I would like now to explain how our proposal achieves all of these objectives:

ACHIEVING SYSTEM SOLVENCY

Our system would make the system solvent for as far as the Social Security Actuaries are able to estimate.

How does it do this? Above all else, it accomplishes this through advance funding.

As the members of this Committee know, our population is aging rapidly. Currently we have a little more than 3 workers paying into the system for every 1 retiree taking out of it. Within a generation, that ratio will be down to 2:1.

As a consequence, if we did nothing, future generations would be assessed skyrocketing tax rates in order to meet benefit promises. The projected cost (tax) rate

of the Social Security system, according to the Actuaries, will be almost 18% by 2030.

The Trust Fund is not currently scheduled to become insolvent until 2034, but as most acknowledge, the existence of the Trust Fund has nothing to do with the government's ability to pay benefits. President Clinton's submitted budget for this year made the point as well as I possibly could:

> "These balances are available to finance future benefit payments and other trust fund expenditures—but only in a bookkeeping sense. . . They do not consist of real economic assets that can be drawn down in the future to fund benefits. Instead, they are claims on the Treasury that, when redeemed, will have to be financed by raising taxes, borrowing from the public, or reducing benefits or other expenditures. The existence of large Trust Fund balances, therefore, does not, by itself, have any impact on the Government's ability to pay benefits."

In other words, we have a problem that arises in 2014, not in 2034, and it quickly becomes an enormous one unless we find a way to put aside savings today. This does not mean simply adding a series of credits to the Social Security Trust Fund, which would have no positive impact, as the quote from the President's budget clearly shows.

What we have to do is begin to advance fund the current system, and that means taking some of that surplus Social Security money today out of the federal coffers and into a place where it can be saved, invested—owned by individual beneficiaries. That money would belong to them immediately, even though they could not withdraw it before retirement. But it would be a real asset in their name.

By doing this, we can reduce the amount of the benefit that needs to be funded in the future by raising taxes on future generations. This is the critical objective, but it allows for flippant political attacks. If you give someone a part of their benefit today, in their personal account, and less of it later on, some will say that it is a "cut" in benefits. It is no such thing. Only in Washington can giving people ownership rights and real funding for a portion of their benefits, and increasing their total real value, be construed as a cut. Accepting such terminology can only lead to one conclusion—that we can't advance fund, because we simply have to be sure that every penny of future benefits comes from taxing future workers. So we need to get out of that rhetorical trap.

Our proposal has been certified by the actuaries as attaining actuarial solvency, and in fact it goes so far as to slightly overshoot. We are "overbalanced" in the years after 2050, and have some room to modify the proposal in some respects and yet still stay in balance.

I would note the consensus that has developed for some form of advance funding. This was one of the few recommendations that united an otherwise divided Social Security Advisory Council in 1996. The major disagreements today among policymakers consist only in the area of who should control and direct the investment opportunities created within Social Security. I believe strongly, and I believe a Congressional majority agrees, that this investment should be directed by individual beneficiaries, not by the federal government or any other public board.

WHY BENEFITS ARE HIGHER UNDER OUR PLAN

We have worked with the Social Security actuaries and the Congressional Research Service to estimate the levels of benefits provided under our plan.

There are certain bottom-line points that should be recognized about our plan. Among them:

1) Low-wage earners in every birth cohort measured would experience higher benefits under our plan than current law can sustain, even without including the proceeds from personal accounts.

2) Average earners in every birth cohort measured would experience higher benefits under our plan than current law can sustain, even if their personal accounts only grew at the projected bond rate of 3.0%.

3) Maximum earners in some birth cohorts would need either to achieve the historical rate of return on stocks, or to put in additional voluntary contributions, in order to exceed benefit levels of current law. However, the tax savings to high-income earners, which I will outline in the next section, will be so great that on balance they would also benefit appreciably from our reform plan.

Under current law, a low-wage individual retiring in the year 2040 at the age of 65 would be promised a monthly benefit of $752. However, due to the pending insolvency of the system, only $536 of that can be funded. We cannot know in advance how future generations would distribute the program changes between benefit cuts

and tax increases. But we do know that our plan, thanks to advance funding, would offer a higher benefit to that individual, from a fully solvent system that would eliminate the need for those choices.

I will provide tables that are based on the research of the Congressional Research Service that make clear all of the above points. The CRS makes projections that assume that under current law, benefits would be paid in full until 2034, and then suddenly cut by more than 25% when the system becomes insolvent. CRS can make no other presumption in the absence of advance knowledge of how Congress would distribute the pain of benefit reductions among birth cohorts. In order to translate the CRS figures into a more plausible outcome, we added a column showing the effects that would come from the benefit reductions under current law being shared equally by all birth cohorts.

Benefit Table #1: The Bipartisan Plan's Benefits Would Be Higher for Low-Income Workers Even Without Counting Personal Accounts

(Assumes Steady Low-Wage Worker) (Monthly Benefit, 1999 Dollars) (Assumes Retirement at Age 65)

Yr	Current Law (Benefit Cuts Begin in 2034)	Current Law Sustainable*	Bipartisan Plan (Bond Rate No Vol. Contrib.)	Bipartisan Plan (w/o Account Benefits)	Bipartisan Plan (w/1% Voluntary Contributions)
2000	626	517	615	606	627
2005	624	515	620	601	645
2010	652	539	698	667	738
2015	673	556	733	687	790
2020	660	545	754	691	832
2030	690	570	776	694	877
2035	512	595	798	693	926
2040	536	621	821	689	981
2050	582	678	869	710	1051
2060	611	739	920	749	1107

*The Congressional Research Service, in the left-hand column, assumes that all of the burden of benefit changes under current law will commence in 2034. In order to produce a more realistic prediction of how the changes required under current law would be spread, the "current law sustainable" column assumes that they have been spread equally among birth cohorts throughout the valuation period.

Benefit Table #2: The Bipartisan Plan's Benefits Would Be Higher for Average-Income Workers Even if Accounts Earn Only a Bond Rate of Return (3.0%)

(Assumes Steady Average-Wage Worker) (Monthly Benefit, 1999 Dollars) (Assumes Retirement at Age 65)

Yr	Current Law (Benefit Cuts Begin in 2034)	Current Law Sustainable*	Bipartisan Plan (Bond Rate, No Voluntary)	Bipartisan Plan (Stock Rate)	Bipartisan Plan (w/1% Vol. Contributions, Bond Rate)
2000	1032	852	1014	1016	1029
2005	1031	852	973	982	1006
2010	1076	889	991	1014	1046
2015	1111	918	977	1024	1057
2020	1090	900	1005	1092	1115
2030	1139	941	1083	1183	1179
2035	845	982	1063	1307	1250
2040	884	1026	1093	1476	1329
2050	961	1119	1157	1672	1442
2060	1007	1221	1225	1778	1531

*The Congressional Research Service, in the left-hand column, assumes that all of the burden of benefit changes under current law will commence in 2034. In order to produce a more realistic prediction of how the changes required under current law would be spread, the "current law sustainable" column assumes that they have been spread equally among birth cohorts throughout the valuation period.

The alternative course is that current benefit promises would be met in full by raising taxes, both under current law and under proposals to simply transfer credits to the Social Security Trust Fund. I have also provided a table that shows the size of these tax costs, and will comment further upon them in the next portion of my statement.

I would like to point out that these figures apply to individuals retiring at the age of 65. Thus, even with the increased actuarial adjustment for early retirement under our plan, and even though our plan would accelerate the pace at which the

normal retirement age would reach its current-law target of 67, benefits under our proposal for individuals retiring at 65 would still be higher.

Our tables also show that the progressive match program for low-income individuals will also add enormously to the projected benefits that they will receive.

WHY TAXES WILL BE MUCH LOWER UNDER OUR PLAN

If there is a single most obvious and important benefit of enacting this reform, it is in the tax reductions that will result from it.

I am not referring to the most immediate tax reduction, the payroll tax cut that will be given to individuals in the form of a refund into a personal account.

The greatest reduction in taxes would come in the years from 2015 on beyond. At that time, under current law—and under many reform plans—enormous outlays from general revenues would be needed to redeem the Social Security Trust Fund, or to fund personal accounts. The net cost of the system would begin to climb. The federal government would have to collect almost 18% of national taxable payroll in the year 2030, more than 5 points of that coming from general revenues.

The hidden cost of the current Social Security system is not the payroll tax increases that everyone knows would be required after 2034, but the general tax increases that few will admit would be required starting in 2014.

With my statement, I include a table showing the effective tax rate costs of current law as well as the various actuarially sound reform proposals that have been placed before the Congress. These figures come directly from the Social Security actuaries. They include the sum of the costs of paying OASDI benefits, plus any mandatory contributions to personal accounts. (Under our proposal, additional voluntary contributions would also be permitted. But any federal "matches" of voluntary contributions from general revenues would be contingent upon new savings being generated.)

Let me return to our individual who is working in the year 2025 under current law. In that year, a tax increase equal to 3.61% of payroll would effectively need to be assessed through general revenues in order to pay promised benefits. As a low-income individual, his share of that burden would be less than if it were assessed through the payroll tax, but it would still be real. Under current law, his income tax burden comes to about $241 annually.

Comparison of Cost Rates of Current Law and Alternative Plans

(As a percentage of taxable payroll)

Yr	Current Law	Archer/ Shaw	Senate Bi-partisan	Kolbe/ Stenholm	Gramm	Nadler
2000	10.8	12.8	12.7	12.9	15.0	10.4*
2005	11.2	13.3	13.2	13.0	15.2	10.6
2010	11.9	13.9	13.4	13.4	15.6	11.2
2015	13.3	15.0	14.0	14.0	16.4	12.5
2020	15.0	16.4	14.7	14.8	17.3	12.8 (14.2)
2025	16.6	17.4	15.4	15.6	17.6	14.4 (15.8)
2030	17.7	17.8	15.7	15.7	17.1	15.5 (16.9)
2035	18.2	17.3	15.5	15.2	16.4	15.9 (17.4)
2040	18.2	16.2	14.8	14.5	15.2	16.0 (17.5)
2045	18.2	14.9	14.3	13.8	14.1	16.1 (17.5)
2050	18.3	13.8	13.9	13.3	13.4	16.3 (17.7)
2055	18.6	13.1	13.7	13.2	13.0	16.6 (18.0)
2060	19.1	12.6	13.7	13.1	12.8	16.9 (18.5)
2065	19.4	12.3	13.6	13.4	12.5	17.1 (18.8)
2070	19.6	12.1	13.5	13.7	12.4	17.3 (19.0)

(Annual cost includes OASDI outlays plus contributions to personal accounts.) Peak cost year in bold

(Figures come from analyses completed of each plan by Social Security actuaries. Archer/Shaw plan memo of April 29, 1999. Senate bipartisan plan (Gregg/Kerrey/Breaux/Grassley et al) memo of June 3, 1999. Kolbe/Stenholm plan memo of May 25, 1999. Gramm plan memo of April 16, 1999. Nadler plan memo of June 3, 1999. Nadler plan total cost given in parentheses, cost estimate given on assumption that stock sales reduce amount of bonds that must be redeemed from tax revenue. Due to construction of plans, cost rates for the Archer/ Shaw, Gramm, and Nadler plans would vary according to rate of return received on stock investments.)

*Tax rate of Nadler plan is lower than current law not because total costs are less but because amount of national income subject to tax is greater. In order to compare total costs of Nadler plan to other plans, cost rate given in Nadler column must be multiplied by a factor that varies through time. This factor would be close to 1.06 in the beginning of the valuation period, and would gradually decline to 1.03 at the end. For example, the tax rate given as 11.2% in 2010 under the Nadler column would equate to the same total tax cost as the 11.9% figure in the current law column.

Part II: Comparison of Cost Rates of Current Law and Alternative Plans

(As a percentage of taxable payroll)

Yr	Current Law	Moynihan/Kerrey
2000	10.8	11.1 (13.1)*
2005	11.2	11.0 (13.0)
2010	11.9	10.9 (12.9)
2015	13.3	11.5 (13.5)
2020	15.0	12.2 (14.2)
2025	16.6	13.2 (15.2)
2030	17.7	13.8 (15.8)
2035	18.2	14.0 (16.0)
2040	18.2	14.0 (16.0)
2045	18.2	14.0 (16.0)
2050	18.3	14.2 (16.2)
2055	18.6	14.5 (16.5)
2060	19.1	14.7 (16.7)
2065	19.4	14.8 (16.8)
2070	19.6	14.9 (16.9)

(Annual cost includes OASDI outlays plus contributions to personal accounts.) Peak cost year in bold

(Analysis of Moynihan/Kerrey plan is based on SSA actuaries' memo of January 11, 1999, and is listed separately because it is the only projection provided here based on the 1998 Trustees' Report. 1999 re-estimates would vary. Unlike the other personal account proposals, the accounts in the Moynihan/Kerrey plan are voluntary. The figure without parentheses assumes no contributions to, and thus no income from, personal accounts. The figure inside parentheses assumes universal participation in 2% personal accounts, for comparison with other personal account plans.)

*Like the Nadler plan, the Moynihan/Kerrey plan would increase the share of national income subject to Social Security taxation, but to a lesser degree. Thus, tax rates will appear lower than would an equivalent amount of tax revenue collected under the Archer/Shaw, Gramm, or Kolbe/Stenholm plans. The correction factor required to translate one cost rate into another would be between 1.03–1.06 for the Nadler proposal, 1.01–1.02 for the Senate bipartisan proposal, and 1.01–1.04 for the Moynihan/Kerrey proposal.

Under our proposal, that tax burden would drop by roughly 37%, from $241 to $153.

Middle and high-income workers would not experience benefit increases as generous as those provided to low-income individuals under our plan. But we have determined that by the year 2034, an average wage earner would save the equivalent of $650 a year (1999 dollars) in income taxes, and a maximum-wage earner, $2350 a year. I want to stress that these savings are net of any effects of re-indexing CPI upon the income tax rates. These are net tax reductions, even including our CPI reforms.

I would also stress that 2025 is not a particularly favorable example to select. Our relative tax savings get much larger after that point, growing steadily henceforth.

A look at our chart showing total costs reveals how quickly our proposal, as well as the Kolbe-Stenholm proposal, begins to reduce tax burdens.

A plan as comprehensive as ours can be picked apart by critics, provision by provision. It is easy to criticize a plan's parts in isolation from the whole, and to say that one of them is disadvantageous, heedless of the other benefits and gains provided. One reason for the specific choices that we made is revealed in this important table. The result of not making them is simply that, by the year 2030, the effective tax rate of the system will surpass 17%, an unfortunate legacy to leave to posterity.

OUR PLAN PROTECTS THE BENEFITS OF CURRENT RETIREES

How would current retirees be affected by our proposal?

Only in one way. Their benefits would come from a solvent system, and therefore, political pressure to cut their benefits will be reduced. Our proposal would not affect their benefits in any way. Even the required methodological corrections to the Consumer Price Index would not affect the benefits of current retirees.

Under current law, there is no way of knowing what future generations will do when the tax levels required to support this system begin to rise in the year 2014. We do not know whether future generations will be able to afford to increase the tax costs of the system to 18% of the national tax base by the year 2030, or whether other pressing national needs, such as a recession or an international conflict will make this untenable. Current law may therefore contain the seeds of political pressure to cut benefits. Moreover, as general revenues required to sustain the system

grow to the levels of hundreds of billions each year, there is the risk that upper-income individuals will correctly diagnose that the system has become an irretrievably bad deal for them, and that they will walk away from this important program.

By eliminating the factors that might lead to pressure to cut benefits, our proposal would keep the benefits of seniors far more secure.

STRENGTHENING THE SAFETY NET AGAINST POVERTY

Poverty would be reduced under our proposal, even if the personal accounts do not grow at an aggressive rate. The reason for this is that our proposal would increase the progressivity of the basic defined, guaranteed Social Security benefit. It would also gradually phase in increased benefits for widows.

Moreover, our plan would protect the disabled. They would be unaffected by the changes made to build new saving into the system. Their benefits would not be impacted by the benefit offsets proportional to personal account contributions. If an individual becomes disabled prior to retirement age, they would receive their current-law benefit.

It is important to recognize that we do not face a choice between maintaining Social Security as a "social insurance" system and as an "earned benefit." It has always served both functions, and it must continue to do so in order to sustain political support. The system must retain some features of being an "earned benefit" so as not be reduced to a welfare program only. This is why proposals to simply bail out the system through general revenue transfusions alone—to turn it into, effectively, another welfare program in which contributions and benefits are not related—are misguided and undermine the system's ethic.

Again, I would repeat that our proposal contains important benefits for all individuals. Guaranteed benefits on the low-income end would be increased. High income earners would be spared the large current-law tax increases that would otherwise be necessary. If we act responsibly and soon, we can accomplish a reform that serves the interests of all Americans.

OUR PROPOSAL WOULD REDUCE UNFUNDED LIABILITIES

By putting aside some funding today, and reducing the proportion of benefits that are financed solely by taxing future workers, our proposal would vastly reduce the system's unfunded liabilities.

Consider such a year as 2034. Under current law, the government would have a liability from general revenues to the Trust Fund equal to an approximately 5 point payroll tax increase. By advance funding benefits, our plan would reduce the cost of OASDI outlays in that year from more than 18% to less than 14%. The pressure on general revenue outlays would be reduced by more than half.

The Social Security system would be left on a sustainable course. The share of benefits each year that are unfunded liabilities would begin to go down partway through the retirement of the baby boom generation. By the end of the valuation period, the actuaries tell us, the system would have a rising amount of assets in the Trust Fund.

OUR PLAN COMBINES THE BEST FEATURES OF MANY REFORM PLANS

Mr. Chairman, I would stress to you that our plan is not the work of any one single legislator. It is the product of painstaking negotiations conducted over several months. The seven names that you see on the proposal are not the only ones who contributed to it. We took the best ideas that we could find from serious reform plans presented across the political spectrum. Each of us had to make concessions that we did not like. But we did this in the interest of reaching a bipartisan accord.

We believe that our plan is indicative of the product that would result from a larger bipartisan negotiation in the Congress. Accordingly, we believe that it provides the best available vehicle for negotiations with the President if he chooses to become substantively involved. It was our hope to put forth a proposal on a bipartisan basis, so that the President would not have to choose between negotiating with a "Republican plan" or a "Democratic plan." Stalemate will not save our Social Security system.

OTHER REFORMS IN THE BIPARTISAN PLAN

The changes effected in our bipartisan bill do not, all of them, relate solely to fixing system solvency.

One area of reforms includes improved work incentives. Our proposal would eliminate the earnings limit for retirees. It would also correct the actuarial adjustments for early and late retirement so that beneficiaries who continue to work would receive back in benefits the value of the extra payroll taxes they contributed. The proposal would also change the AIME formula so that the number of earnings years in the numerator would no longer be tied to the number of years in the denominator. In other words, every year of earnings, no matter how small, would have the effect of increasing overall benefits (Under current law, only the earnings in the top earnings years are counted towards benefits, and the more earnings years that are counted, the lower are is the resulting benefit formula.)

We also included several provisions designed to address the needs of specific sectors of the population who are threatened under current law. For example, we gradually would increase the benefits provided to widows, so that they would ultimately be at least 75% of the combined value of the benefits that husband and wife would have been entitled to on their own.

We also recognized the poor treatment of two-earner couples relative to one-earner couples under the current system. Our proposal includes five "dropout years" in the benefit formula pertaining to two earner couples, in recognition of the time that a spouse may have had to take out of the work force.

WHAT OUR PROPOSAL DOES NOT DO

Unveiling a proposal as comprehensive as ours invariably creates misunderstanding as to the effect of its various provisions.

First, let me address the impact of our reforms on the Consumer Price Index. Most economists agree that further reforms are necessary to correct measures of the Consumer Price Index, and our proposal would instruct BLS to make them. Correcting the CPI would have an effect on government outlays as well as revenues. This is not a "benefit cut" or a "tax increase," it is a correction. We would take what was incorrectly computed before and compute it correctly from now on. No one whose income stays steady in real terms would see a tax increase. No one's benefits would grow more slowly than the best available measure of inflation.

However, we wanted to be doubly certain that any effects of the CPI change upon federal revenues not become a license for the government to spend these revenues on new ventures. Accordingly, we included a "CPI recapture" provision to ensure that any revenues generated by this reform be returned to taxpayers as Social Security benefits, rather than being used to finance new government spending. This is the reason for the "CPI recapture" provision in the legislation.

Our proposal would not increase taxes in any form. The sum total of the effects of all provisions in the legislation that might increase revenues are greatly exceeded by the effects of the legislation that would cut tax levels. The chart showing total cost rates makes this clear.

Our provision to re-index the wage cap is an important compromise between competing concerns. Fiscal conservatives are opposed to arbitrarily raising the cap on taxable wages. The case made from the left is that, left unchanged, the proportion of national wages subject to Social Security taxation would actually drop.

Our proposal found a neat bipartisan compromise between these competing concerns. It would maintain the current level of benefit taxation of 86% of total national wages. This would only have an effect on total revenues if the current-law formulation would have actually caused a decrease in tax levels. If total wages outside the wage cap grow in proportion to national wages currently subject to taxation, there would be no substantive effect. This proposal basically asks competing concerns in this debate to "put their money where their mouth is." If the concern is that we would otherwise have an indexing problem, this proposal would resolve it. If the concern is that we should not increase the proportion of total wages subject to taxation, this proposal meets that, too. I would further add that the figure we choose—86%—is the current-law level. Some proposals would raise this to 90%, citing the fact that at one point in history it did rise to 90%. The historical average has actually been closer to 84%, and we did not find the case for raising it to 90% to be persuasive. Keeping it at its current level of 86% is a reasonable bipartisan resolution of this issue.

CONCLUSION

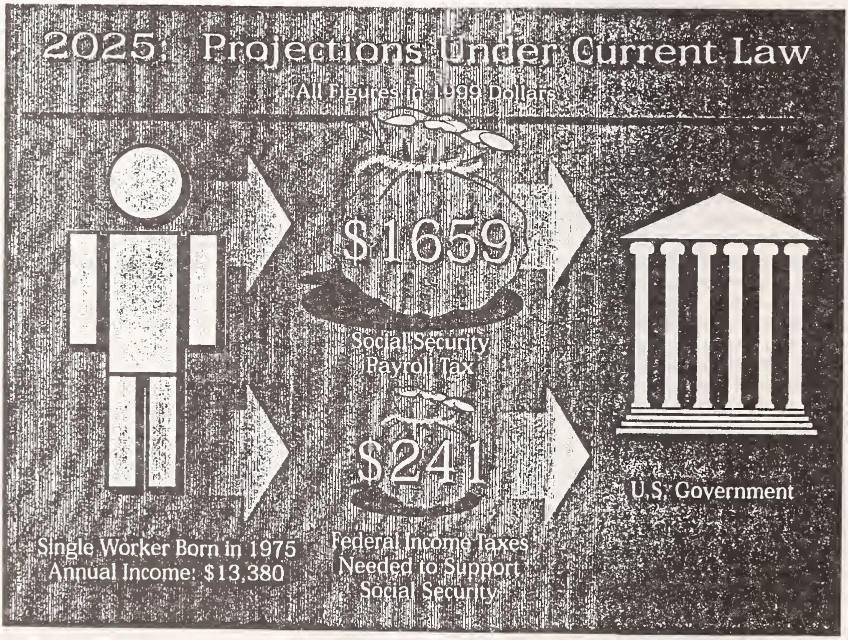
Mr. Chairman, I thank you once again for using your position of leadership to advance debate on this important issue. I appreciate your courtesies in inviting us to testify. I do hope that you and the rest of this Committee will look at the total effects of our plan in evaluating what it would achieve. I am confident that in doing so, you will find that it is a reasonable basis for hope that we can achieve a bipar-

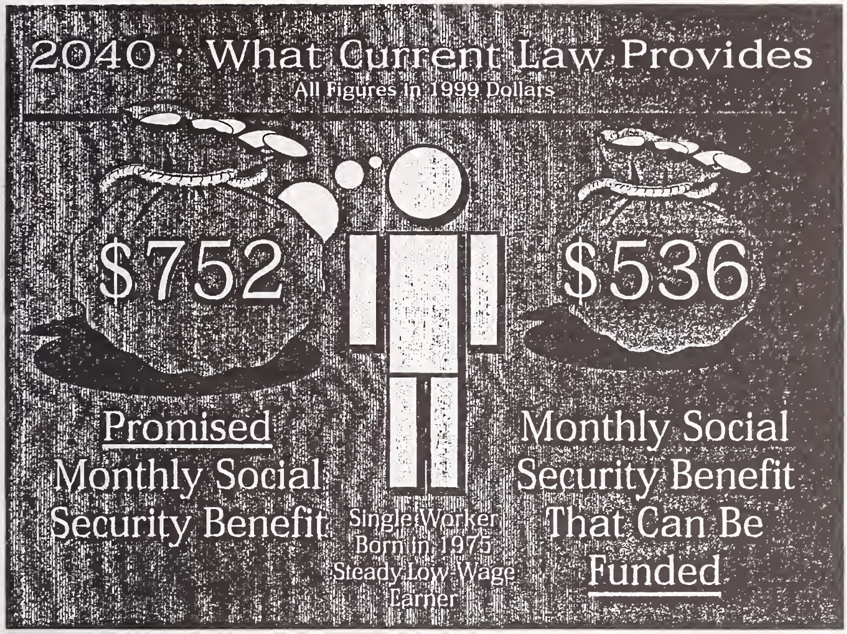
tisan agreement. I thank you again and would be pleased to answer any questions that you may have.

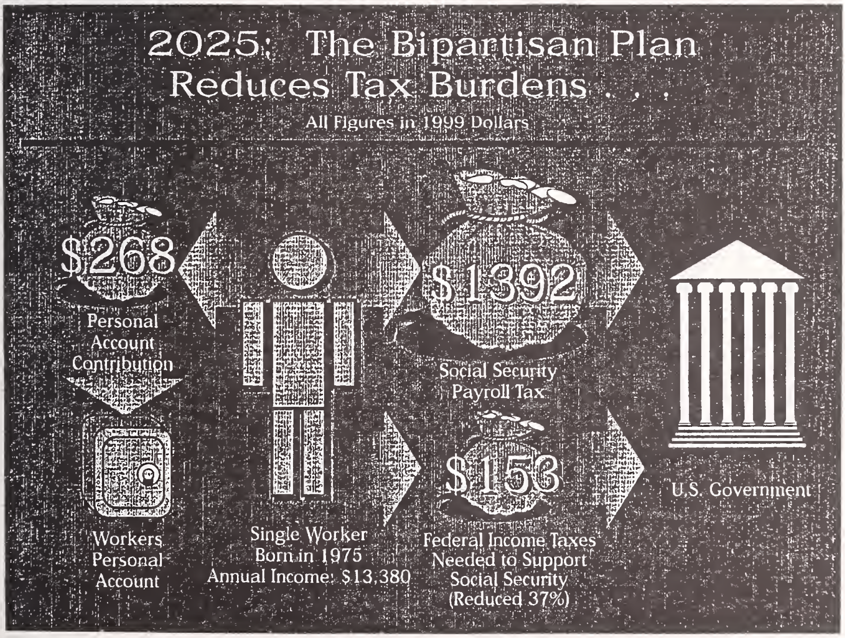
The Bipartisan Agreement: Something For Everyone

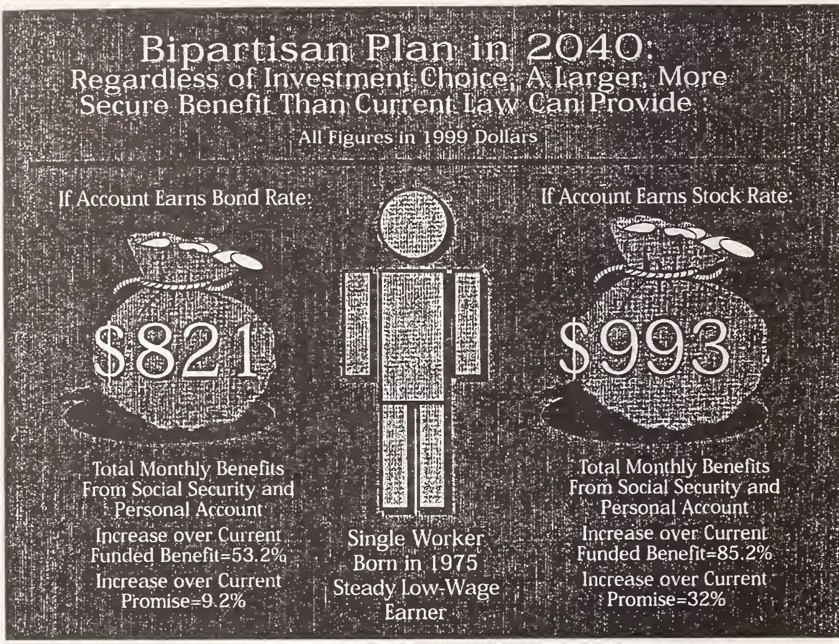
Low-Wage Earners	Average Earners	High Earners
-Increases of up to 31% over promised benefits and up to 91% over what current system can fund*	-Increases of up to 18% over promised benefits and up to 69% over what current system can fund*	-By 2034, eliminates more than $2350/year in income taxes needed to fund Social Security benefits
- A progressive match program to increase value of voluntary contributions	-Savings of more than $650/year in income taxes by year 2034	- Guarantees Social Security benefits above what current system can permanently fund

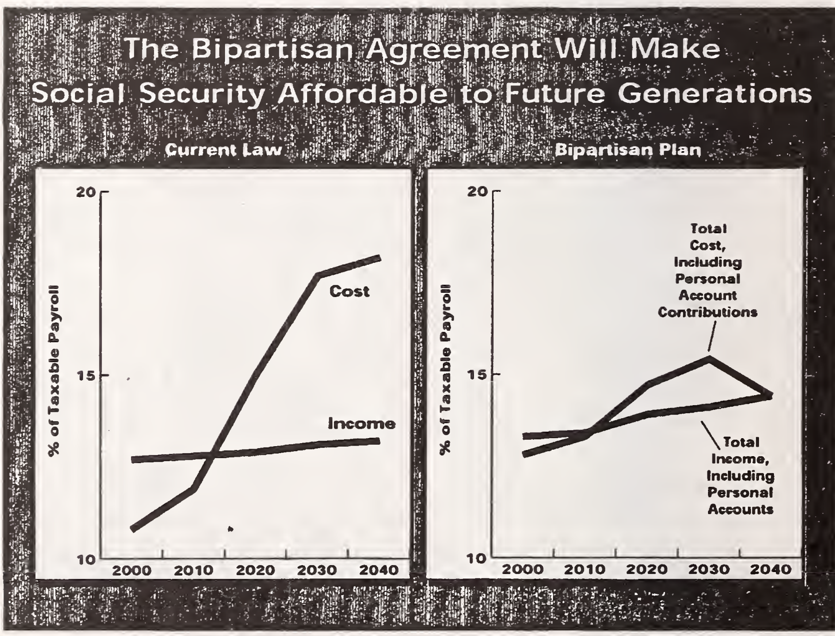
*-High Figures assume stock return rate and completed transition to new system (all figures in 1999 dollars)

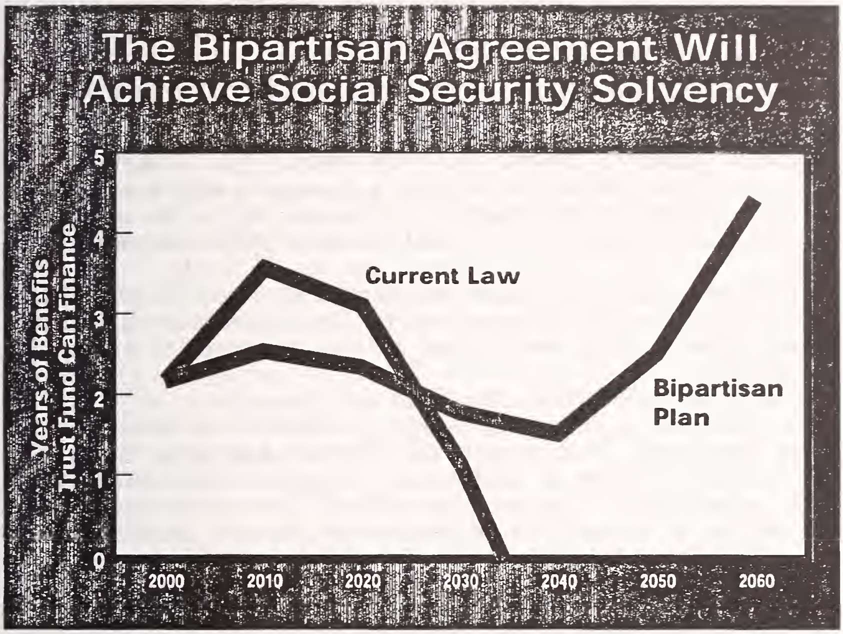


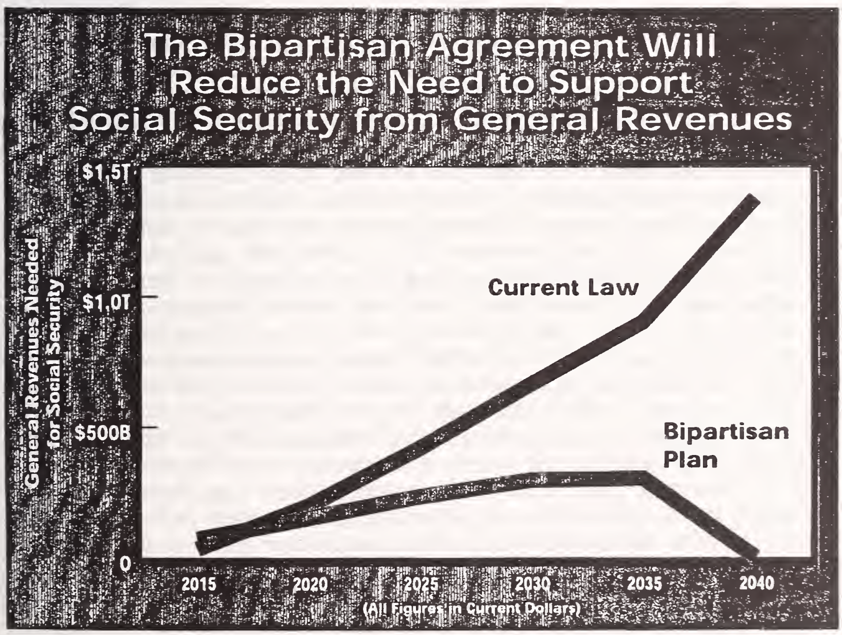

2040 : What Current Law Provides
All Figures in 1999 Dollars
$752
$536
Promised Monthly Social Security Benefit
Single Worker
Born in 1975
Steady Low-Wage
Earner
Monthly Social Security Benefit That Can Be Funded


2025: The Bipartisan Plan
Reduces Tax Burdens . . .
All Figures in 1999 Dollars
$268
Personal
Account
Contribution
$1392
Social Security
Payroll Tax
$153
U.S. Government
Workers
Personal
Account
Single Worker
Born in 1975
Annual Income: $13,380
Federal Income Taxes
Needed to Support
Social Security
(Reduced 37%)


Bipartisan Plan in 2040:
Regardless of Investment Choice, A Larger, More Secure Benefit Than Current Law Can Provide
All Figures in 1999 Dollars
If Account Earns Bond Rate:
$821
Total Monthly Benefits From Social Security and Personal Account
Increase over Current Funded Benefit=53.2%
Increase over Current Promise=9.2%
Single Worker Born in 1975 Steady Low-Wage Earner
If Account Earns Stock Rate:
$993
Total Monthly Benefits From Social Security and Personal Account
Increase over Current Funded Benefit=85.2%
Increase over Current Promise=32%


The Bipartisan Agreement Will Make Social Security Affordable to Future Generations
Current Law
% of Taxable Payroll
20
15
10
Cost
Income
2000 2010 2020 2030 2040
Bipartisan Plan
% of Taxable Payroll
20
15
10
Total Cost, Including Personal Account Contributions
Total Income, Including Personal Accounts
2000 2010 2020 2030 2040





Mr. SHAW. I would ask the witnesses, would it be better to go to Senator Grassley now, since he was part of your bill?

Senator GREGG. We are all together on the same bill.

Mr. SHAW. Oh, Senator Kerrey is, too? Fine, then I will recognize Senator Kerrey, excuse me.

STATEMENT OF HON. J. ROBERT KERREY, A U.S. SENATOR FROM THE STATE OF NEBRASKA

Senator KERREY. Thank you very much, Mr. Chairman and Members of the Committee. I have a statement that I would just ask to be included in the record as well as a copy of an evaluation the Chief Actuaries of the Social Security Administration have made.

Mr. SHAW. Chairman Archer announced at the early part of this hearing that the full statements of all the witnesses will be made a part of the hearing and invited all the witnesses to proceed as they see fit.

Senator KERREY. I thank the Chair for that.

Let me make a couple of points in addition to what Senator Gregg has already done. First of all, there are two forks in the road that we have to take as Members of Congress. Fork number one is: Do we act today or do we delay reform? Do we wait until tomorrow, defined as some other odd-numbered year, or should we wait until 2034 when the system runs completely out of money? Everybody who has evaluated this problem, whether they are on the left or on the right, reaches the conclusion that the sooner we address the problem, the smaller the problem is. The longer you delay, the worse either the cuts in benefits are going to be or the higher the increases in taxes are going to be. And unlike Medicare, this is a fairly simple problem to solve. This is not one where any staff member would have a great deal of difficulty presenting reform options to a Member. There is not a complicated set of facts to deal with here.

The question really is, are you willing to go to your citizens in your congressional district or in your State and tell them the truth: If you are under the age of 45, we have a promise on the table that we can't keep. All discussions of Social Security options—we have one that we have introduced—need to be debated in the context of the actuaries' statement that if you are under the age of 35, there will either be a 25- or a 33-percent reduction in benefits awaiting you or a similar increase in payroll taxes to accommodate the benefits that we currently promised to people who are under the age of 45. These are really the facts that we are dealing with here.

There really aren't an awful lot of options here to choose from. We either take action now or we delay action and increase the size of the problem in the future. No matter when you enact reforms, it is going to be difficult to do. Whether you propose reforms behind the shield of a Commission's recommendation or you do it in an odd-numbered year when it is more favorable for electoral reasons, there will always be plenty of reasons not to enact reforms because when you look at the options, none of them are very politically attractive—whether it is a tax increase or a benefit reduction or some combination. Our proposal does not favor a tax increase. I note the President doesn't either. He doesn't think we should increase payroll taxes. There may be some in Congress who favor a tax increase. Let them put their proposal on the table. I think delay is

the worst option of all. Those who are arguing "Well, let us wait until next year or the year after," are arguing for steeper cuts in benefits or steeper increases in taxes. Those are the only two choices available to you.

The second fork in the road is a key one for me, especially as a Democrat, and that fork is: Do you want Americans, when they are eligible for an old-age benefit or a survivor or a disability benefit—in our proposal, we leave the survivor and the disability benefit just as it is. About 20 percent of all beneficiaries use the survivor and disability benefit; we leave that alone. We are talking in our proposal only about an old-age benefit, and 1.1 million of 1.4 million Americans who took that benefit in 1997 took it at age 62, 63 or 64 so it is an old-age benefit that we are talking about here.

No matter when you take that benefit, the question that creates another fork in the road is "Do you want people to be more dependent upon the government for their retirement and their old-age needs, or do you want them to be less dependent on the government?" Our proposal takes the fork that says we want them to be less dependent based upon the belief that in addition to a defined benefit, which we retain, that the source of real independence that comes in old age comes from ownership of financial assets. We believe it is a mathematical certainty that if you start at an early enough age, that regardless of what your wage is, whether you are making $7 an hour or $700 an hour, that it is possible for you, indeed, I would argue, desirable, for you over the course of your working life to accumulate ownership of financial assets and wealth.

Oftentimes, you will hear people say, "The rich are richer, and poor are getting poorer" and then propose to increase the minimum wage. Well, income and wealth are not the same things, and so this proposal says in addition to making certain that all beneficiaries are covered, we will give them the opportunity to create wealth. Under current law, what we do is we run the trust funds balance up to a very high amount and in 2014 and over the next 20 years we draw the trust funds down. To draw them down means you have to redeem the IOUs by using incomes taxes and corporate incomes taxes; that is how it is done. You are not going to replace the IOUs with additional debt; you are going to redeem them by using income from corporate income and individual income taxes over the next 20 years until the trust funds are insolvent. Under our proposal, the trust fund ratio never drops down below 100 percent of a single year's benefits. It starts at 193 percent; by 2074, the trust fund ratio is over 500 percent. So, all beneficiaries will get the promise that we already have on the table. The second fork in the road, and you can design it any way you want, is whether or not you want Americans to have more financial security as a consequence of owning financial assets. This proposal answers that question emphatically. Yes.

There are a number of specific changes in our proposal, Mr. Chairman and Members of the Committee, that I would like to identify, and I will try to identify them quickly. They are included in my more lengthy statement that I have already, Mr. Chairman, introduced into the record. Let me deal, first of all, with the benefit cuts. Again, as I said, we have opted not to increase payroll taxes.

Some Members may. Some Members may honestly say, "No, let us raise payroll taxes." We say, "No, we don't want to increase payroll taxes." We achieve security in the future for beneficiaries by making a number of changes in the benefit structure. We increase the benefit computation period for up to 5 additional years for newly eligible retirees. Lower earning or two-earning couples will get 5-year extra dropout years in anticipation that one spouse may have taken time out of his or her career for child rearing. We maintain the taxable wage base at 86 percent. We credit all revenue from the taxation of OASDI benefits to the OASDI Trust Fund. We reward work by increasing the size of early retirement factors and delayed retirement credits.

Next, we use a more accurate cost of living adjustment for all programs affected by the consumer price index; that is a 0.5 percent change in the consumer price index calculation. In addition, any revenues generated as a result of the COLA adjustment will be recaptured for the OASDI Trust Fund.

Last, we eliminate the hiatus years in increasing the retirement age to 67, and we index the benefits. We do not move eligibility age beyond 67. We keep the eligibility age exactly as it is, but by eliminating the earnings test, it becomes a true old-age benefit, no longer a retirement benefit. You don't have to retire to get this benefit. It is an old-age benefit. You can take it at 62; you can take it at 65. It is adjusted under current law to 67. We eliminate the hiatus period, and we adjust the benefits according to life expectancy increases thereafter.

Mr. Chairman and Members of the Committee, again, as I said, there are a limited number of reform options. We have made the choice to make reductions in outyear liabilities. There are no changes in benefits for people over the age of 62. No one should go out and interview somebody over the age of 62 and ask them "What do you think about the reduction in benefits that Senator Kerrey is proposing?" No reduction in benefits will occur for any currently eligible beneficiary.

All of these changes, Mr. Chairman and Members of the Committee, enable us to do two things. One, as I said, keep the promise that we have on the table to all beneficiaries, whether you are eligible today or whether you are going to be eligible in the future. According to the actuaries of the Social Security Administration, our reform proposal restores solvency to the program; it is an actuarial balance for as far as the eye can see beyond 2074. To every beneficiary that is alive today, whether you are 1 year of age or 62 years of age, we can keep the promise that we have on the table.

The second thing we do is we establish an opportunity for individual beneficiaries to accumulate wealth over the course of their life. I emphasize this, Mr. Chairman. The goal is not to create savings accounts; that is a means to the end. The end is to increase financial independence, to provide people with real financial security by allowing them, through the Social Security system, to accumulate wealth. Our plan offers a 2 percent payroll tax contribution, which is an effective reduction in payroll taxes. Our plan also includes a government savings match that allows wage earners of $36,000 or less to contribute at least $726 a year. We believe that

is necessary in order to take advantage of compounding interest rates.

Our plan opens an account of $1,000 at birth and contributes $500 for each of the first 5 years of life. The most important variable in accumulating wealth is the length of time over which you save the money. We believe, therefore, that it is necessary to open those accounts at as early an age as possible, and we make it possible for individuals to contribute an additional unmatched, aftertax $2,000 to their account every single year.

Mr. Chairman, Members of the Committee, I emphasize what I said at the beginning: there are two choices that we have as Members of Congress. One, we can take action now or we can delay. Many people are saying, "Let us delay." Mr. Chairman, I appreciate more than I can say your leadership in saying that we have got to act now, because if you don't, the problem gets worse.

Second, the next fork in the road is do you want Social Security to become a source of wealth and financial security? I believe we are better off having people who are in the work force saying that at some point when they become eligible, they are going to be less dependent on the government, not more dependent on the government for their postwork needs, and that is what our proposal does.

Mr. Chairman and Members of the Committee, I would like to make one further comment. Lots of people are saying, in both the Republican and the Democratic party, that we ought to have a lockbox proposal. I have got great respect for both Democrats and Republicans that have their versions of the lockbox, but, as all of us know who have looked at this thing, it is going to be similar to when Geraldo Rivera opened Al Capone's safe on national television. They are going to open the thing up 30 years from now, and there is not going to be anything in it. This lockbox is a way for us to postpone action. It is a way for us to say, "Well, we want to get beyond this next election, and then we will deal with it when we are more secure politically in some way, shape, or form."

So, again, I appreciate very much, Mr. Chairman, your leadership in this in saying that we cannot delay; that we should take action sooner rather than later, and I hope that our proposal or some proposal like it becomes the law of the land rather soon.

[The prepared statement follows:]

Statement of Hon. J. Robert Kerrey, a U.S. Senator from the State of Nebraska

Thank you, Mr. Chairman, for giving me the opportunity to come before the Committee to talk about the Bipartisan Social Security Reform proposal. I appreciate your ongoing interest in and commitment to reforming the Social Security program. This hearing provides an important opportunity to outline the major differences between different approaches to Social Security reform.

I am delighted to be here today with Senators Breaux, Gregg, and Grassley to talk about our bipartisan plan to reform Social Security. Our goal was to put together a bill that would achieve actuarial solvency and reduce programmatic liabilities in a way that improved the retirement security of women and low income workers and did not affect current retirees. The proposal we are here to discuss today is the fruit of these discussions.

Mr. Chairman, I would like to begin my remarks by making a comparison between seismologists and politicians. In seismology, scientists look at a calm, stable surface and know that massive tectonic plates are moving slowly below the surface in directions that portend the inevitable arrival of an earthquake. Seismologists are trained to examine the small shifts underneath our ordinary lives. Through these examinations, they predict when the extraordinary moments will arrive.

Thus are seismologists and elected politicians separated by the habits of our ways. For in our lives as politicians, we are encouraged to give priority attention to the details of life on the surface. The tectonic plates are rarely our concern until and unless they produce an earthquake.

Social Security insolvency is one example of a slowly-building public policy earthquake shifting beneath the surface of our every day lives—waiting to create a fiscal crisis in 2034. The actuaries at the Social Security Administration—the political equivalent of seismologists—have the technical capability to warn us years in advance about the extraordinary demographic events that will cause earthquakes of the "public policy crisis" variety. Most recently, the actuaries have predicted that massive demographic movements will begin to occur in ten years and last for the next 20 years. During that time period, the number of Americans eligible for an old-age Social Security benefit will increase from 37 million to 77 million, while the number of working Americans whose wages will be taxed to pay these benefits will only increase from 137 million to 145 million.

Barring a sudden and large increase in productivity, the actuaries tell us this massive demographic shift will produce an unavoidable conflict between eligible beneficiaries and those whose wages are taxed to pay the benefits. In 2034, some future Congress will be forced to choose between reducing benefits or increasing taxes by 25 to 33 percent. The longer Congress waits before changing the law, the more painful these tax increases and benefit cuts will be.

There are at least two more demographic shifts quietly taking place which affect the programmatic costs of the Social Security program. First, Americans are living longer. When the Social Security program was created in 1935, life expectancy was 60 for men and 65 for women. Today, the average male will live to 73 and the average female to 80. In 2030, men and women will live to 77 and 82.4, respectively. Life expectancy for those who live to age 65 is even longer. Life expectancy for these healthy American men and women is 80 and 84 today, and will be 84 and 86 in 2030.

A second trend is that beneficiaries are taking their old age benefit earlier in life. In 1997, 1.1 million of the 1.4 million new beneficiaries opted to take reduced benefits under the early eligibility program. Most people take early, reduced benefits because they know that if they live to age 72, they will earn back all of the benefits they lost through the reduction.

Let me mention some of the other trends that add to the urgency for Congress to act. First, there is a growing gap between the wealthiest and the poorest Americans. Secondly, the number of Americans for whom Social Security is 90% or more of their old age income is growing. This means that a large number of workers—including the vast majority of low income workers—are depending on Social Security for their sole source of income at retirement. This trend is particularly disturbing in light of the fact that the household savings rate among low and middle income and younger workers is so low.

The urgent need for reform only becomes more obvious if we look at the impact of our inaction on future workers and retirees. The reason we are trying to keep Social Security solvent for 75 years, is to keep the Social Security promise to all beneficiaries—current and future—who are alive today. Simply keeping the system solvent for 35 years—and letting the Trust Funds become insolvent—means trouble for workers who are 45 years of age or younger. Failure to act soon will have dire consequences for these current workers.

Recently, seven members of the Senate—three Democrats and four Republicans—announced a proposal that would restore solvency to the Social Security program. This proposal preserves the current disability and survivors benefit programs—currently used by 13.7 million Americans. In addition, this proposal will impose no benefit reduction on any beneficiary age 62 or over, eliminates the earnings test for retirees who continue to work, and does not increase the payroll tax. The proposal will close the wealth gap and give low income workers a substantial boost in creating and accumulating wealth. Not only will our proposal boost the account contributions of low income workers, but our plan also increases the traditional defined benefits of lower income workers by increasing their replacement rate. Furthermore, our proposal will improve the Social Security benefits of widows.

Individual Accounts: The Centerpiece of the Bipartisan Social Security Reform Plan

New individual savings accounts owned by the beneficiary are the most important and least understood portion of our proposal. These accounts are not an end in themselves. They are a means to an end. The purpose of these accounts is threefold: 1) to close the wealth gap; 2) to decrease dependency on the Federal government

for financial security in retirement through increased ownership of financial assets; and 3) to reduce future unfunded liabilities by prefunding a portion of a worker's Social Security benefit. The individual accounts portion of our proposal has four components:

1. Starting in 2000, workers will divert 2 percentage points of their payroll (FICA) tax contributions into an individual savings account. Workers will choose from among several broad-based investment funds administered like the Federal employees' Thrift Savings Plan (TSP).

2. Low income workers will have the opportunity to boost their account contributions by participating in a government match program. The match works as follows:

• For the first dollar of savings, qualified workers will get an automatic government contribution of $100.

• Beyond the first dollar of personal savings, each qualified worker will get an additional dollar-for-dollar match from the government.

Qualified workers include all workers whose 2% contribution is less than 1% of the taxable wage base ($726 in 1999)—this would allow all workers earning less than $36,300 in 1999 to participate in the savings match program. The sum total of the 2% contribution, the $100 grant, and the dollar-for-dollar match may not exceed 1% of the taxable wage base ($726).

3. All workers will have the opportunity to add an additional $2,000 of after-tax savings to their individual accounts each year.

4. KidSave accounts will be opened for all children at birth with a $1,000 contribution. An additional $500 will be added to the KidSave account for each of the first five years of life. The goal of the KidSave accounts is to maximize retirement savings accumulations by allowing all workers to save over a longer period of time.

The impact of these wealth accounts for lower and middle income workers will be dramatic. Regardless of their hourly wages, workers will be able to create substantial amounts of wealth and establish financial independence by taking advantage of the magic of compounding interest over a long period of time. If our proposal became law this year, fifty years from today a new generation of Americans would be heading towards their retirement years with more wealth, security, and independence.

Consider the impact on a male baby born in 1999 who grows up, graduates in high school in 2017, enters the work force after graduation at an inflation adjusted $7 per hour, and remains there for forty five years. Under current law that individual would be eligible for a defined benefit only; under the proposed change that individual would be eligible for a defined benefit plus a private annuity from their wealth account.

At $7 per hour, this individual's annual salary would be approximately $13,500. If Congress cuts benefits in 2034, this future retiree would receive a monthly benefit check worth $428.

Under our proposal, this individual (taking early retirement) would receive a monthly benefit check worth at least $644 if he invested at the low-risk, low-return bond rate. If he took advantage of a higher rate of return, he could expect to see a monthly benefit of $775. If he chooses to participate in the government savings match program and uses his KidSave account to supplement his monthly income, this low-income individual will have an even higher monthly benefit.

Programmatic Adjustments in the Bipartisan Social Security Reform Plan

Our proposal also calls for making several programmatic changes that will improve widows benefits, increase the defined benefit for low-income individuals, and contain programmatic costs. These changes include:

1. Establishing a new bend point in the PIA formula factor which will boost benefits and increase the replacement rate for low income workers.

2. Increasing the widow(er)'s benefit formula so that widow(er)s will eventually receive 75% of the combined benefit of both spouses.

3. Eliminating the retirement earnings test for all individuals age 62 and older.

4. Increasing the benefit computation period for up to 5 additional years for newly-eligible retirees. However, the lower earning of a two-earner couple will get five extra "drop-out" years, in anticipation that one spouse may have taken time out of his or her career for child-rearing.

5. Maintaining the taxable wage base at 86%—the current percentage of wages subject to the Social Security payroll (FICA) tax. Rather than letting the taxable wage base float with the annual percentage growth in wages, this new formulation will permanently keep the taxable wage base at 86% of wages.

6. Crediting all revenue from the taxation of OASDI benefits to the OASDI trust funds by 2014. Currently, retirees earnings over $34,000 ($44,000 for couples) must

pay taxes on 85% of their benefits. The income from the taxes on the first 50% of their benefits goes to the OASDI funds, while the remaining tax revenue flows into the HI Fund. This provision ensures that all Social Security tax dollars stay in the Social Security program.

7. Rewarding work by increasing the size of early retirement factors and delayed retirement credits.

8. Using a more accurate cost-of-living adjustment (COLA) for all programs affected by the Consumer Price Index (CPI). This COLA adjustment (.5%) will *not* be applied to the benefits of any workers or retirees currently age 62 and older. In addition, any revenues generated as a result of the COLA adjustment will be "recaptured" for the OASDI Trust Funds.

9. Creating a life expectancy index. To reflect both past and future increases in life expectancy, our proposal would eliminate the hiatus years in increasing the retirement age to 67 and would index benefits to life expectancy thereafter.

This proposal boosts benefits, reduces taxes, and ensures that large portions of our discretionary budget will not be needed to pay Social Security benefits. The sponsors of this proposal believe that time is not on our side. Delay will hurt those who rely on Social Security the most. Delay will only allow the problem to become larger—and the solution more difficult. Delay is especially devastating for Americans who would benefit if the law made it possible for all workers to share in the American dream of financial independence through ownership of financial assets.

What we are not willing to accept is political inaction—inaction despite the full knowledge that the tectonic plates are shifting dangerously below us. These shifts will cause an earthquake in the not too distant future, an earthquake which will destabilize the financial security of tens of millions of American working families. Unlike the destruction of a geologic earthquake we have the power to prevent this one. The sponsors of the Bipartisan Social Security Reform Plan intend to do all we can to see that this Congress acts sooner rather than later.

We welcome helpful suggestions on how to improve our proposal. I look forward to answering any questions that the Committee may have.

Chairman ARCHER [presiding]. Senator, thank you. Thank you for your presentation, and thank you for your being out front on this issue. I certainly do agree with you. We need to act, and we need to act this year, and I am just hopeful that we can find a way to do that, but my same compliments extend to all four of you, because all four of you have been willing to get out front and to design a plan that does save Social Security for 75 years. Some say, "Oh, well, that is not necessary," but, frankly, we ought to be extending that with the life expectancy going up to where we are projecting for 80 or 85 years instead of the 75 that has been traditional. But for right now, we will work with the 75, and I do compliment all of you.

Senator Grassley.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA, AND CHAIRMAN, SPECIAL COMMITTEE ON AGING

Senator GRASSLEY. Well, I need to compliment you, because your legislation moved the ball forward quite a bit on this side of the hill, and each of us Senators in our respective forums have had an opportunity to do that. Senator Breaux and I have worked together as Chairman and Ranking Member of the Aging Committee. We have had six hearings on Social Security reform. I have had an opportunity to serve with Senator Moynihan as Cochair of the Americans Discuss Social Security.

I want to concentrate on that area that Senator Gregg has suggested that I have been having my main interest in and that is eco-

nomic justice for women. I believe that the bipartisan plan which we support addresses women's needs, and so I would explain it this way: Women are more likely to move in and out of the work force to care for children or elderly parents. They should not be punished for the time that they dedicate to dependents. Our proposal provides five drop-out years to the spouse with lower earnings in every two-earner couple.

Women, on average, earn less than men. Our proposal provides all workers with an opportunity to contribute to their individual accounts an amount equal to 1 percent of the taxable wage base. For this year, that would be $726. Workers with combined 2 percent contributions of less than 1 percent of the taxable wage base would receive $100 from the U.S. Treasury. Furthermore, they will receive a dollar-for-dollar match by the government on voluntary contributions up to 1 percent of the wage base. Also, our proposal creates an additional bend point to the benefit formula to boost the replacement rate for low-income workers.

Women live longer than men. At age 65, men are expected to live 15 more years, whereas, women are expected to live almost 20 years. Our proposal addresses that reality by allowing money accumulated in the individual accounts to be passed on to surviving spouses and children. Furthermore, our proposal would increase a widow's benefit to 75 percent of combined benefits that a husband and wife would be entitled to based on their own earnings.

As many older Americans lives longer, healthier lives, as well, they are eager to remain in the work force in various capacities. Others remain in the work force out of necessity. We would eliminate the earnings test for beneficiaries age 62 and older so that retirees may continue to contribute to the economy without being penalized. Currently, benefits are reduced for over 1 million beneficiaries, because their wages exceed earnings limits.

Our proposal would also correct the actuarial adjustment for early and late retirement. As you know, individuals do not receive back the value of payroll taxes contributed if they delay their retirement. This proposal increases both the early and delayed retirement adjustments to levels appropriate to recognize additional tax contributions. Retirees who remain in the work force could also contribute to their individual accounts.

The first step on the road to reforming Social Security was to engage the American public in a policy debate. No action could take place without Americans being able to make informed decisions about how to design a Social Security Program which would meet the needs of the next century. Now, America is ready for reform. According to a recent poll brought about by the Americans Discuss Social Security, 58 percent of those sampled feel that reform should take place before the year 2000 election.

The second step in saving Social Security, is the funding problem that the system faces. Several proposals have been put forward to save Social Security. Now we must work together in that next step and that is enacting legislation that restores the long-term solvency of Social Security.

I must stress the importance of saving Social Security sooner rather than later. Do we work now to prepare for the retirement of the baby boomers and subsequent generations or do we just sit

back and end up, as we have been, seemingly unprepared for the long term? According to Social Security actuaries, in 2075, the last year of the 75-year evaluation period, income to the Social Security Program will be $14 trillion, but we will owe $21 trillion in benefits, and, obviously, you can't take more hay out of the barn than you put into that barn. Plain and simple, that translates into stiffer reforms that will need to be made for each year that we don't enact legislation to protect the program so many Americans rely upon.

So, I thank you for this opportunity and for your leadership, Chairman Archer, on this proposal and for having this hearing. I would be happy to entertain any questions after Senator Breaux.

[The prepared statement follows:]

Statement of Hon. Charles E. Grassley, a U.S. Senator from the State of Iowa; and Chairman, Senate Special Committee on Aging

Thank you Chairman Archer. I am pleased to have the opportunity to be here today with my colleagues from the Senate to discuss our bipartisan proposal to save Social Security. I want to commend you and your colleagues on the Committee for holding this hearing. It is an important step on the road to reforming Social Security.

My colleagues have thoroughly outlined the proposal we have put together. I think it is worth restating some of its positive points. Our proposal does not raise the payroll tax. It gives middle and low income workers the opportunity to create wealth. It works to protect the members of our society who are most vulnerable and dependent on the Social Security system. And, most importantly it restores the long-term solvency of the program that millions of retired and working Americans and their families rely on to provide the basis for their retirement income security.

There are a few specific aspects that I would like to highlight. In putting together this proposal, this group has been very conscientious of how changes to the Social Security system would affect different populations. As we have moved forward in the process to reform Social Security, one group that I have been particularly concerned about is women. In February, the Aging Committee, which I chair and of which Senator Breaux is the ranking member, held a hearing examining how women would be affected by an individual account component. One of the things that came out of that hearing was that, while women's needs from the Social Security system are magnified compared to men's because of their longer life spans and different work patterns, those issues can be addressed as part of a reformed system. I believe the bipartisan plan which my colleagues and I support addresses the needs of women. Let me explain how:

Women are more likely to move in and out of the workforce to care for children or elderly parents. We recognize that there is a high likelihood that a spouse may take time away from work to raise children or care for elderly parents. They should not be punished for the time that they dedicate to dependent family members. Under our proposal, five "drop out" years would be provided to the spouse with lower earnings in every two-earner couple.

Women, on average, earn less than men. Our proposal provides all workers with an opportunity to contribute to their individual accounts, at a minimum, an amount equal to one percent of the taxable wage base. One percent of this year's taxable wage base, which is $72,600, would be $726. Wage earners whose combined two percent contribution is less than one percent of the taxable wage base will receive a $100 contribution by the federal government when they make their first voluntary contribution of $1. Furthermore, they will receive a dollar-for-dollar match by the government on voluntary contributions up to a total equal to one percent of the wage base.

In addition, our proposal creates an additional bend point to the Social Security formula to boost the traditional Social Security replacement rate for low-income workers. Under current law, beneficiaries receive 90 percent of the first $505 of their average indexed monthly earnings, plus 32 percent of their average indexed monthly earnings over $505 through $3,043, plus 15 percent of their average indexed monthly earnings over $3,034. Our proposal would create a new bend point so that there would be a 90 percent bend point, a 70 percent bend point, a 32 percent bend point and a 15 percent bend point. This would enhance the traditional Social Security benefit for low and middle income workers.

Women live longer than men. At age 65, men are expected to live another 15 years, whereas women are expected to live almost 20 more years. One way in which our proposal addresses that reality is by allowing money accumulated in the individual accounts to be passed on to surviving spouses and children. Furthermore, our proposal would increase the widow's benefit to 75 percent of the value of the combined benefits that a husband and wife would be entitled to based on their own earnings.

Developments in modern science allow many older Americans to live longer, healthier lives. Their minds are sharp and they are eager to remain in the workforce in various capacities. Others remain in the workforce out of necessity. Our proposal would eliminate the earnings test for all beneficiaries age 62 and older so that retirees may continue to contribute to the American economy without being penalized. Under the current earnings test, benefits are reduced for over one million beneficiaries because their wages exceed the earnings limit.

Our proposal would also correct the actuarial adjustment for early and late retirement. As you are already aware, under current law, individuals do not receive back the value of extra payroll taxes contributed if they delay retirement. This proposal increases both the early and delayed retirement adjustments to the level appropriate to recognize additional tax contributions. Of course, retirees who remain in the workforce will also be able to continue to contribute to their individual account.

The first step on the road to reforming Social Security was to engage the American public in the policy debate. No action could take place without the citizens of the country being able to make informed decisions about how to design a Social Security program which would meet their needs in the 21st Century. We dedicated last year to a year of debate about Social Security reform. The Administration, members of Congress and many organizations held forums, roundtables, and seminars on Social Security reform in an effort to engage the American public in this critical debate. Now, the American public is ready for reform. According to poll results released by Americans Discuss Social Security last month, 58 percent of those sampled feel that Social Security reform should take place before the 2000 elections.

The second step in saving Social Security was to develop proposals which address the future funding problems our Social Security system will face. As is evident today by the witnesses at this hearing, several proposals have been put forward to save Social Security. Now we must work toward the next, and possibly most difficult, step: enacting legislation which will restore the long-term solvency of the Social Security program.

I want to stress the importance of saving Social Security sooner rather than later. There is a famous fable about an ant and a grasshopper. The ant worked tirelessly during the warm summer to prepare for the long winter. The grasshopper did nothing to prepare. We are at a point where we as Congress and a nation must decide whether we are going to be ants or grasshoppers: whether we are going to work now to prepare for the retirement of the baby boom generation and subsequent generations, or whether we are going to sit back and end up being unprepared.

Just eight years from now, the first year of the baby boom generation will be eligible to collect early retirement benefits. Seven years after that, when those retirees are just 69 years old, the Social Security program will run a deficit of $49 billion and the federal government will be forced to start calling in those IOU's. According to the actuaries at the Social Security Administration, in the year 2075—the last year of the 75-year actuarial time horizon—income to the Social Security program will be $14 trillion, however, we will be obligated to pay $21 trillion in benefits. Plain and simple, that translates into stiffer reforms that will need to be made for each year that goes by and we don't enact legislation to protect the program that so many older Americans rely on.

Chairman ARCHER. Thank you, Senator Grassley.

Senator Breaux.

STATEMENT OF HON. JOHN B. BREAUX, A U.S. SENATOR FROM THE STATE OF LOUISIANA

Senator BREAUX. Thank you, Mr. Chairman and Members of the Committee. I am delighted to be here. I will tell you that I have been to the Ways and Means Committee more times this morning than I did in the 14 years that I was in the House of Representa-

tives. This is my third visit over here, but I am delighted to have the opportunity to share some thoughts with you, and I congratulate you all for doing this. I can't think of anything more difficult than sitting and listening to a bunch of other Members of Congress talk about Social Security and what our plans are to reform it. So, I congratulate all of you for taking the time to do it. This is not an easy exercise, and we have all sat on that side and listened to ourselves talk, and it is very, very difficult.

The conventional wisdom is that you can't fix Social Security this year, because next year is an election year, and, obviously, if you follow that line of thinking, you can't fix it next year, because it is an election year. So, with that line of thinking, we will never do anything to fix a problem that affects not just the 40 million Americans who are on the program, but their children, their grandchildren, and generations to come. So, I congratulate all of you for taking the time and for listening to those who have plans and ideas about what to do.

And I will start off by saying that I happen to believe that this can be a win political process for everybody. I mean, good policy is good politics, and if we are not smart enough to sell good policy to our constituents as being good politics, then we are all in the wrong business. What we cannot continue to sell is failure, and what I think that we as a Congress—both sides are guilty of this in Medicare and Social Security, alike—we blame each other for failures. "It is their fault we didn't pass anything." "No, it is their fault we didn't do anything." "No, it is your fault, because you didn't run the program properly." "No, it is your fault, because you want to gut the problem." So, we have been arguing for several years now about whose fault it is that nothing has been done. And I would suggest that the American people are really getting pretty tired of that argument. They are starting to say that all of you people up there can't get anything done, because you are worried about who is going to get the credit and who is going to get the blame.

So, I think that we have a unique opportunity, Mr. Chairman and Members of the Committee, that this year will be a little bit different in that we can come together. You are not going to write a program that only Democrats can vote for that is ever going to become law, and you are not going to write a Republican plan that is ever going to become law as long as you have a Democratic President who says, "I can't accept some of the things that you have in it." I mean, the need is obvious that we are going to have to come together and work on things that we don't totally agree with but is good public policy, and then we can go back and say, "Look what we did." And we can argue about who is going to get credit for it, but that is a much better argument arguing about success than arguing about blaming the other side for failure. It is better to argue about success than it is to argue about failure and whose fault it is.

What we have today—and I am not going to get into details, because I think my colleagues probably did it much better than I am capable of doing it—but we have the only bipartisan plan, Republicans and Democrats. We have the only bicameral plan. We have got Jim Kolbe and Charlie Stenholm who are going to follow I

think, and they are going to present the same thing that we are presenting. It has got some things in it that Democrats are not going to like, and it has got some things in it that Republicans are not going to like, but it does represent the House and the Senate, Republicans and Democrats offering something that I think makes sense.

And I congratulate you, Mr. Chairman. You have put something out on the table. I mean, you have been willing to say, "OK, we are going to have something out there," and we have done the same thing. We have all been willing to say, "OK, we are going to go first. Here it is, take a shot at it, but do something with it. Just don't say we are not going to do anything."

I think that one of the real features of our plan is the 2 percent in individual retirement accounts that we mandate people establish, and it is not a novel approach. It is what every one of you have. It is what everyone behind you has in the Federal Thrift Savings Plan. They put money in the Thrift Savings Plan. They can pick a low option, a low risk, a high risk, or a medium risk. It is managed by a private investment group, and they pick the investments. A low risk is government bonds; a medium risk is a combination of bonds and also the stock market, and a high risk is the stock market, S&P 500 market. And they pick and choose, and it has been very successful.

It is, I think, impossible to totally privatize the system. I would oppose it. Some people think it is the right thing to do. It is not going to happen. It is not going to happen in this political atmosphere. Others argue, "Well, don't do anything, and we will just wait it out and hope that it cures itself," and that it is irresponsible. So, there is something in between making it all private and doing nothing with regard to private investment that I think is acceptable, and that is what we have recommended, and we say 2 percent is invested in individual retirement accounts. They can own it; they can inherit it, and one of the big differences is they keep what they make.

I think your plan, Mr. Chairman, suggests that, well, if you have a private investment account and that what you get you reduce your Social Security benefits as a result of what you got from your private account. We reduce it by the amount that you would have gotten had you kept it in the Social Security system at 3 percent return, but you get the extra, so there is an incentive to save. You want to put it in the individual account, because you know that you will actually make more money from your account if you invest it appropriately and properly. It is not the government investing, but is also the individuals doing it through a professional group that would manage the money just like we have in the Thrift Savings Plan for the Federal employees.

We have a CPI correction. That is how we partially finance it, and I think that is important to make it be reflective of what the real consumer price index gets, and I think that is the right way to go.

So, anyway, I just would say, I mean, thank you for listening to us, and thank you for listening to all the other Members; that has got to be brutal. I know we have done it on our side, and it is brutal. But thank you all for being here, and I just think that we

ought to maybe this year try and do something differently from what we have been doing and get a plan that makes sense that is not perfect from a Democratic perspective, and it is not perfect from the Republican perspective, but it is a heck of a lot better than we have right now, and I would suggest that what we have offered I think meets that criteria. Thank you very much.

[The prepared statement follows:]

Statement of Hon. John B. Breaux, a U.S. Senator from the State of Louisiana

We will all soon face the formidable task of revamping the cornerstone of American social policy—Social Security. I believe the proposal our bipartisan group has put forth is a step in the right direction. In 1935, Social Security began as part of the bold vision of President Franklin D. Roosevelt. He argued that this country demands "bold, persistent experimentation," challenging future improvements for Social Security. As we face reform, the question is whether to just restate this sacred contract or seize an opportunity to "persist" with the vision and experiment of Social Security.

It is time for both. President Roosevelt viewed Social Security as "development towards that goal, rather than a finished product...we should be constantly seeking to perfect and strengthen it in the light of our accumulating experience and growing appreciation of social needs." After 63 years of Social Security, the task falls to us all to ask: Is this the best we can do to provide Americans with economic security?

The driving force propelling the Social Security debate is that comprehensive reform *must* happen in 1999. For both economic and political reasons, everyone agrees that next year will present a rare and limited window for reform. If this time frame is viewed in earnest—as it should be—there is no time for partisan bickering, rhetorical battles or demagoguery. We must immediately move to build a consensus through realistic, centrist solutions.

It is my belief that there are four corners of Social Security reform: Individual Accounts; Increased Progressivity; Strengthening the Disability Program; and Fiscal Responsibility. Within these four corners, consensus can be found between Democrats, Republicans and the American people. Our plan was guided by these four corners.

Individual Accounts

If we are not careful, we will run recklessly into massive gridlock between individual accounts versus collective investment. This will make reform in 1999 impossible, and we will have failed in our responsibility to reform Social Security.

Gridlock is avoidable. The concept of creating opportunities for equity investment through individual accounts—if done properly—can achieve a middle ground by combining the best of both worlds.

Experts agree that equity investment has a proper role in a long-term, prudent retirement strategy. This fundamental economic advice is true at every income level. Equity investment and the magic of compound interest should be available to every American. If not, these individuals will only be pushed further into the fringe of the economy. We are supposed to bring to an individual's doorstep opportunities that our capitalist markets alone will not provide.

The goal of Social Security is to provide economic security to those at the bottom of the economic pyramid. In 1935, during an era of economic hardship, we chose to do that through a system that redistributes wealth. This foundation of social insurance must be maintained, but Social Security should emerge from reform ready for the post-industrial, global economy. We should accept Roosevelt's challenge not to look at Social Security as a finished product, but as development of the goal. Shouldn't we do more than simply sustain those on the fringe of economy? Shouldn't we help bring these Americans into the economic mainstream?

While an objective of individual accounts is to expand investment options, there is more at stake. If we offer the opportunity for equity investment to the government, not individuals, we miss an opportunity to evolve the Social Security system. Adding individual accounts to Social Security builds upon the social insurance by providing individuals with a direct link to economic advancement. This is the policy that will reaffirm and reconnect the American people's faith in Social Security.

Increased Progressivity

Our individual accounts do not lessen Social Security's progressivity. In our reform proposal, we increase progressivity through several provisions, including bend points changes and matching contributions for low and middle income workers. A low-income worker's individual account would be purely a bonus above their traditional benefit.

As we rush to protect economic security in old age, we can not ignore that the most effective way to provide economic security is to provide economic development throughout a lifetime.

Strengthening the Disability Program

One-third of Social Security beneficiaries are not retirees, but disabled Americans. The disability program is essential to the safety net and it is in the worst financial shape. It, too, must be strengthened and modernized.

The disability program must be examined in the context of overall reform, yet its policy issues are not necessarily linked with retirement policy. The retirement aspect of Social Security actually lends itself to a broader look at pension and personal savings policies that the Congress must address.

The disability program is part of a complex web of federal and state programs. Issues spilling over into Medicare, Medicaid, SSI and vocational rehabilitation will all need thoughtful examination. We should move to establish the appropriate forum to debate and discuss disability issues.

Fiscal Responsibility

There are several components to real, honest fiscal responsibility. First, we must not depend on projected budget surpluses to fix Social Security or to fund "no pain" solutions. Let's be clear, we have no budget surpluses. Projected budget surpluses remain a largely unrealized victory. A recession could wipe out more than half the projected surpluses.

There is a danger in our message on Social Security—the public may believe "save the surplus for Social Security" is the equivalent of saying "the surpluses will save Social Security." Worst yet, some policy makers may actually start to believe this. The next century will bring varying economic scenarios and Social Security will have to withstand them all.

Real Social Security reform requires tough choices. Sending any other message to the American people is wrong. If we spend one dime of an unrealized surplus to avoid making a politically tough, but necessary choice—it will be nothing short of a lie to the American people.

We also must look beyond solvency. Even if Social Security's books were balanced, an unrestructured program would absorb nearly 18 percent of income subject to payroll taxes, up from the current 12.4 percent. The unfunded liabilities of Social Security nears $3 trillion and will have to be paid with taxes not yet collected. We must protect future generations and tomorrow's economy from this daunting tax burden.

Finally, it is irresponsible to jeopardize other priorities because we do not have the political will to make difficult decisions. Continued economic growth depends upon increased productivity. Increased productivity depends upon a growing labor force and greater worker output. But, labor force growth has slowed dramatically with little chance of reversing, so we must rely on greater productivity.

Increasing a worker's productivity means investing in training, education, health and nutrition as well as technologies and infrastructure. These investments are even more critical as America's workforce becomes more racially and ethnically diverse, because historically minorities have not had the same access to health, education and training.

We will soon face a momentous collision of financial pressures. Entitlement spending is bearing down on the federal budget. This crowds out dollars for other discretionary investments, just when these investments will be needed to counter changes in the labor market and continue economic growth. We must properly prepare for this collision by balancing all policy priorities, not by simply increasing revenues to entitlement programs.

I am confident that within these four corners of reform, we can find a centrist, bi-partisan solution to live up to our responsibility to reform Social Security in this Congress.

Senator GREGG. Mr. Chairman. I apologize, I am going to leave. I am marking up my appropriations bill, which has a minor item called the census amendment that I know there is some interest in on your side.

Chairman ARCHER. Senator, you are excused, and I am sure you will be adequately represented by the three remaining colleagues of yours.

Senator GREGG. Very much so. So, I thank you for your courtesy.

Chairman ARCHER. Thank you for coming.

Senator Breaux, it is not difficult to listen on a subject that is as important as this is and particularly where there are people who are genuinely interested in trying to find solutions and not just some sort of a political niche. I think more of us have got to join in that frame of mind in that approach.

Having said that, all plans are subject to some criticism and some reservations and some ways of saying, "Oh, but what about this and what about that?" But there are some things about your plan that are different that I would like to be able to inquire about. You do cut benefits, which distinguishes you a little bit, probably significantly, from a lot of other plans. At least based on AARP's evaluation of what is a benefit cut, you cut benefits, and perhaps that is the direction to go, but it is nevertheless an essential part of your plan to make it work. When you reduce the CPI, Consumer Price Index, you do it only for new retirees, as I understand it.

Senator BREAUX. We do it for anybody who is adjusted for CPI, including the income tax indexing is adjusted, as well, and it doesn't affect anyone 62 and over.

Chairman ARCHER. I understand. So, that would be only——

Senator BREAUX. But it is not just retirees. It is also other parts of the Federal Government that uses the CPI.

Chairman ARCHER. Right. I was going to get to that. But when you reduce the CPI, for my first line of inquiry, you reduce it only for new retirees, not for those who are currently retired.

Senator BREAUX. That is correct.

Chairman ARCHER. And I remember having lived through 1977 and Sunday morning and referred to what we did then. And I was terribly troubled about the notch problem that was going to be created, and I argued against what the Congress did and voted against that bill. We have suffered ever since then from the notch problem, much of which is misunderstood but nevertheless has been a big, big item in our town meetings, and I know you have run into the same thing over the years. Are you not creating another notch problem?

Senator BREAUX. By accurately reflecting the inflation index?

Chairman ARCHER. No, no. By leaving the current CPI in place for current retirees and then in 1 year using a different CPI for people who retire thereafter. You are going to end up with two different benefit levels, I believe, unless I am misreading this, for people with the same earnings record, and I worry about another Dear Abby column which will once again unleash a new notch group on the Congress of the United States.

Senator BREAUX. Well, I think the rationale for doing it the way we did it, Mr. Chairman and Members, would be to say that those who are already receiving retirement benefits would be receiving their increases based on what it was when they got into the system. Whereas, new people who are not yet into the system but know that when they get there that the CPI adjustment would have taken place for them, it is also a political recognition that I don't want all the seniors who are now on it being reduced and take political heat that is unnecessary. I mean, there is a little bit of political reality as well as saying that if you are there now you are going to stay with this, but when you come into the system in the future you will know that you will come in a more accurate CPI cost of living index. I mean, that is just the reason.

Senator KERREY. Excuse me, if I could—do you mind me adding to the——

Chairman ARCHER. No, go ahead.

Senator KERREY. First of all, you are quite right. For future benefits, we are making reductions, but two additional points need to be made. First of all, under current law, there is a 25 to 33 percent cut in benefits. So, one of the things that is in our favor is the tax increase. They would prefer just to increase current taxes by 2 percent, which is $80 billion a year. So, fine, let them make that point; they favor a tax increase. Anybody that does not want current law reduction of benefits to occur out in 2034 has to propose an alternative, and if they don't want to reduce the benefits in 2034, they have got to produce a tax increase.

Those are the only two choices that you have got, it seems to me, unless you use a different way of funding of Social Security, as I believe both you and Congressman Shaw have done with your proposal. There are different ways of funding Social Security. To keep only the defined benefit program, you have a reduction in benefits that occurs under current law.

The second thing is, by changing the bend points for a lower wage individual as our plan does, low-income workers will have an increase in benefits $1,000 to roughly $2,000 a month, as a consequence of adding that additional bend point. I urge you, especially for consideration to Democratic Members who very often talk about their concern for low-income people, the current Social Security Program is not very generous for a low-income individual. It is not very generous at all, and one of the reasons there is an urgency to change the system to increase the capacity of the low-income person to own assets in this country is that it is a pretty cruel hoax to say to somebody "Don't worry about your old-age years, you are going to have Social Security there for you." Because all Social Security does is replace 90 percent of the first $505, and after that, it replaces 32 percent of the next $2,500. Now, that means if you are making $1,000 a month, average indexed monthly earnings, you are going to have about $600 a month in benefits. That hardly allows you to live in the lap of luxury.

So, our plan adds an additional bend point, so for significant numbers of Americans with low- to middle-income wages, they will have not a cut in benefits in the future; it will be an increase in their benefits, in their defined benefit that they get from the Social Security Trust.

Chairman ARCHER. Senator, I understand that, but listening to both of you is deja vu to me to what I listened to in 1977. Almost identically—particularly what Senator Breaux said—almost identical to what I listened to in 1977, and I said, "Wait a minute. Irrespective of all of that logic, all of that reasoning, you are going to end up with beneficiaries who have the same earnings record who are going to be retired at the same time, who are going to be getting different benefits."

Senator KERREY. Mr. Chairman, I respectfully disagree. I was answering the first part of your question, and in the interest of time, not trying to answer the second. But I respectfully disagree. I do not believe that this proposal creates a notch. In 1977, what we were doing is unwinding two COLAs, and we phased one of them out, and that unquestionably created a notch. In this proposal, we are saying that we are going to make this CPI adjustment out in the future.

Chairman ARCHER. But the result will be the same, Senator, because for those people who are currently retired, they will get a CPI under current law. For those who retire in the future, they will get, as they continue their retirement, a lower CPI increase every year, and they will end up having a lower benefit on the same earnings record as people who were already retired, and I can guarantee you, you are going to get deluged with a notch problem again.

Senator KERREY. But, Mr. Chairman, under that logic, we have a huge notch in 2034, because everybody is going to have a 25 to 33-percent reduction in benefits.

Chairman ARCHER. Well, of course, the reason we are here is to try to solve that problem, but——

Senator KERREY. Well, look, I think you can make modifications in our proposal so that you don't end up with a notch.

Chairman ARCHER. But I just want to make you aware that that will come back and bite future Congresses, because the Congress in 1977 did not accept what I urged them to do, which was to freeze the COLA on the retirees that had gotten the unintended benefit until they were where they should be, and there would have been no notch.

Senator KERREY. Mr. Chairman, we made this change and to get rid of this proposal in this fashion, I guess you could apply it and say, "Gee, let us apply the CPI change to current beneficiaries." We just——

Chairman ARCHER. Well, I am not suggesting you do that. I am just pointing out——

Senator KERREY. Well, that is the only way to solve it.

Chairman ARCHER. Well, no, there are—in our bill, we don't change it for any retiree. So, there are other ways to solve it. I just point that out, and I know all these programs can be adjusted, and as we work through this, hopefully we will find common ground, but Senator Breaux, you were also about to say that this change in the CPI does not affect just future Social Security retirees. It affects the tax rates; it affects——

Senator BREAUX. It affects everything that uses CPIs.

Chairman ARCHER [continuing]. The food stamps; it affects everything that we do.

Senator BREAUX. Yes, it all should be accurate.

Chairman ARCHER. But it is a legislated fix in the CPI.

Senator BREAUX. Right.

Chairman ARCHER. And it would also involve a significant tax increase on low- and middle-income people who get hit the hardest by not getting the full indexation that the current law provides.

Senator BREAUX. It merely says they should be indexed correctly.

Chairman ARCHER. Well, but whose judgment is right? If it is legislated, then it is an arbitrary decision as to what it should be.

Senator BREAUX. Mr. Chairman, every expert that testified before the Finance Committee has said that they currently overestimated, and 0.5 percent is sort of a middle type of adjustment. I mean, I can't go defend that somebody should be getting an index benefit more than what it should be.

Senator KERREY. And I would add that if Boskin had come back and said we were underestimating by a point, there would have been 535 votes for it.

Senator BREAUX. No question about it.

Chairman ARCHER. Well, gentlemen, there are many, many other questions that can be asked, because you have a comprehensive program. I am going to——

Senator KERREY. Do you still welcome us here in front of the Committee, Mr. Chairman?

Chairman ARCHER. I am going to quit—[Laughter.]—but I am going to recognize other Members who might have questions.

Mr. Thomas.

Mr. THOMAS. Thank you, Mr. Chairman. I think I am the appropriate one to ask this because of the past history that is on the record and of the various provisions that you have in your package. At least, Senator Breaux and Senator Kerrey, we spent a lot of time wrestling with the Medicare question, and you have a provision in here which in fact takes an amount of money. I don't want to go into the history of whether that was ever appropriate or not; we have to deal with where we are today and that is a transfer of OASDI funds to the Medicare Trust Fund, and you propose a phase-out of that money, and it is about $100 billion over 10 years.

And, by the way, Mr. Chairman, if we haven't already thanked them, I would love to thank again the SSA actuaries for providing us with materials which allow, not only an understanding of each plan but an ability to walk across plans in a way that makes this very difficult job, if I could say so, easier, if not more enjoyable, in this, in the way they broke it down in terms of the actuarial balance or impact on the payroll tax of a 0.32 percent of taxable payroll over the 75 years.

So, that is all a lead-up to the obvious question: Have you abandoned our effort on fixing Medicare? Where are we going to go with the need to deal with this revenue that otherwise would be in place? Or am I not so excited about your Social Security plan because we have got a $100 billion hole in Medicare if we go with that one? So, what is your response?

Senator BREAUX. I think the short answer, Congressman Thomas, is the fact that Social Security tax benefits are intended for Social Security, and what is happening now we are shifting a little bit over into the HI Trust Fund part A, and it is about $6.7 billion

or $6.9 billion out of $400 billion. That is not an insignificant portion, but it is relatively small compared to the total amount of Medicare, and our argument is that Social Security taxes should be used to fund Social Security.

Mr. THOMAS. Philosophically, I agree with you. Do we have any response to $100 billion hole over the 10 years?

Senator BREAUX. Yes. I will pass the Breaux-Thomas Medicare reform bill.

Mr. THOMAS. Thank the gentleman for understanding the direction I was looking for him to go—[Laughter.]

And, Mr. Chairman, I have no further questions.

Chairman ARCHER. Mr. Shaw.

Mr. SHAW. Mr. Chairman, I won't take my full 5 minutes. I want to congratulate this panel on some of the innovative work that they have done in helping to bring this process forward in a bipartisan way in the Senate. I think that I have problems, whether you call it a notch or whether you just call it using a different cost of living index, I can see problems of somebody who is 75 years comparing his check with somebody who is 65 years old somewhere or 67-year-olds down the line. I also think that one of the problems that we have to address is the question that we know each generation pays in more than the generation before it into the Social Security Trust Fund, and I think that we have got to be sure that there is also opportunity for greater return for greater investment.

So, I think that is something that we have to look at very carefully, whether it be modifications to your plan or the acceptance of the Archer-Shaw plan. However, I think that we have to be very careful in working through this process that we don't let the perfect be the enemy of the good, because we have got to—I mean, this thing is a disaster. I think Senator Kerrey, you were absolutely correct when you were talking about the ultimate notch is doing nothing. I mean, it is just like taking a hand grenade, pulling the pin, and giving it to our grandkids. It is a horrible, horrible thing.

Senator, you and Senator Gregg also made mention of the question of exactly what is in the trust fund, and I think it is one of the things that all of us have to be very careful to carefully analyze and see through. The problem is that the trust fund is certainly full of the most secure assets that you can possibly own in the world today being government Treasury bills; nevertheless, when they are owned by the government, itself, they are "I owe me's," which really mean that the taxpayer is on the hook, and we have got to keep our eye on the year 2014 or 2015 when that trust fund starts to have to cash in those Treasury bills in order to continue its obligations. It is very obvious that the effect would be the same with or without those Treasury bills being in there except that the Treasury bills are a very strong commitment of the government to the people who have paid into the accounts. The effect on the taxpayer is exactly the same, and the effect on the beneficiary is exactly the same as if they were not there.

So, I think we have to be very, very careful to keep our eye on that and quit talking about 2035, because 2015 is the date where this whole thing turns south on us, and we have the crisis. So, the crisis is 15 years out there; it is not 35 years out there as some people would have us believe, and I think you have certainly cor-

rectly recognized the problem, and I compliment the four of you for moving ahead boldly as you have.

Senator KERREY. Congressman, I could not agree more with you, and one of the reasons I objected to the President's proposal with Social Security is that he takes a problem that we currently have right now and makes it a virtue. By that, I mean, what happens from 2012 to 2034 is that the Treasury—unlike what is happening right now which is that payroll taxes are higher than necessary to pay beneficiaries—from 2014 to 2034, in order to write monthly checks, Treasury will have to redeem those special issue Treasury bonds. The redemption transaction will occur by using individual income taxes and corporate income taxes to pay Social Security bills; that is the transaction. That is what will happen when those bonds get converted into cash. For 20 years, we are going to be funding more and more and more Social Security checks with individual and corporate income taxes. That means less money for defense and nondefense spending. It means a growing share of the individual and corporate tax resources are going to be transfered to old-age survivor and disability beneficiaries. What the President proposed to do is dramatically increase those general revenues, not only over that 20-year period but for an additional 15 years beyond it.

Mr. SHAW. So, the urgency——

Senator KERREY. So, you are quite right. There is a huge problem, and when we cross over and we start to have to redeem those bonds, the light bulb is going to come on and they will say, "My God, now I understand why this is a problem, because I have got to pay those benefits with individual and corporate income taxes."

Mr. SHAW. And we have got 15 years in which to frontload these things and solve the problem so that our kids can look forward to at least, if not a better retirement than we have today, and I——

Senator KERREY. Just to extend this a bit longer, one of the reasons I held up the actuaries analysis—and I believe your and the Chairman's proposal does a very similar thing—is that our proposal funds it in perpetuity. You don't have this buildup and then drawdown as current law does. You eliminate that problem, though we do it somewhat differently than you do. But the net effect is the same, and I quite agree, as well—let us not let the perfect be the enemy of the good. We ought to be able to say jointly that we insist that we take action sooner rather than later. We may have a difference of opinion on how it ought to be done, but the sooner we get a bill—a markup opportunity so they can start moving something to the floor, the better off we are going to be.

Mr. SHAW. Yes, sir. Thank you.

Senator KERREY. Thank you, Mr. Chairman.

Chairman ARCHER. Senator, and what you have just pointed out is definitely true and a massive difference between your plan and Congressman Stark's plan, which he presented earlier—I think Senator Breaux was here when he did—which shows a massive decline, bigger and bigger and bigger, year by year, as you go out, even though it is certified for 75 years to be OK because it is front end loaded, and it seems to me that we should be seeking something that will provide stability and security that people can count on that begins to get better as time goes on.

I have to interject one comment, because on behalf of, I think, honesty in reporting, the Social Security Trust Fund has never been the cause of debt. I think all of us understand that. The Social Security Trust Fund has never required borrowing on the part of the Federal Government. What is required borrowing has been the deficit in the general Treasury. If the Social Security Trust Fund did not own these bonds—which are characterized by some as "I owe me" and really something we shouldn't consider, because they have got to be paid off by the same people, and so forth—if the Social Security Trust Fund did not own those bonds, they would be owned by the general public, because the debt would have to be financed. The debt from the general Treasury has to be financed, and it would still have to be paid off by future taxpayers.

So, I just think—I know it is good to say, "Oh, there is nothing in the trust fund and all that, and a lot of people believe that and, therefore, let us go on and present ourselves to the way people believe instead of facing the reality," and in the end, we have to face that reality, and I compliment you for the fact that I think you are facing reality.

And I also agree that I really hope we can mark up a bill this year, because it will not get easier; it will get tougher, and Congressman Shaw and I do not have a magic answer to the problem, and what we have presented certainly can be adjusted in certain ways provided that we do the long-term job and that we do it with a regard for the unified budget surplus so that we do not destroy that and that we do it with regard, hopefully, to having reduction in taxes over the long term, and if we do it, hopefully, without cutting any benefits.

But I thank you. Does any other Member wish to inquire?

Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman.

I am a little confused right now on the COLA adjustment. In reading the testimony of one of you—and I can't remember which one it was—I got the impression that your plan does not make an explicit reduction in the COLA but only mandates that the Bureau of Labor make an adjustment to reflect the actual rate of increase in the cost of living. But then I read in some other documents where you have an explicit 0.5-percent reduction. Which is it?

Senator BREAUX. It instructs them, Jim, to come back with an adjustment in the CPI of 0.5 percent.

Mr. MCCRERY. OK, so your legislation assumes that the inaccuracy in the current COLA is 0.5 percent——

Senator BREAUX. That is correct.

Mr. MCCRERY [continuing]. And you mandate that BLS make that change.

Senator BREAUX. That is correct.

Mr. MCCRERY. OK. Are your individual accounts connected to Social Security? Do they reduce Social Security benefits?

Senator BREAUX. It is a good question. I think it is important to understand what we have done with the individual accounts, because it is a 2 percent set aside for an individual retirement account, and they pick, like we do in the Thrift Savings Plan, where they want to put it. When they retire, that is their account. They can inherit it; they can pass it on to their children; it belongs to

them. Their Social Security benefits would be reduced only to the extent that 2 percent stayed in the regular Social Security retirement plan at about a 3-percent rate of interest. It would be reduced by that amount, but you would get everything extra that you got in your Thrift Savings Plan.

Mr. McCRERY. OK.

Senator BREAUX. If you had gotten a 15-percent return, you would have it reduced by 3 percent, but you would get the extra 11 percent.

Mr. McCRERY. So, there is a so-called clawback to the extent of——

Senator BREAUX. Only to the extent——

Mr. McCRERY [continuing]. What it would have earned in Treasury.

Senator BREAUX. That is correct. It doesn't wipe it out, for instance, which I think is very important. If you have people encouraging them to save, you want to make sure they can keep the benefits of what they save.

Senator KERREY. If I could add, Congressman, in addition CRS and the Social Security actuaries have told us that low-wage earners in every birth cohort measured would experience higher benefits under this plan. Average earners in every birth cohort measured would experience higher benefits under the plan than current law can sustain even if their personal account only grew at the projected rate of 3 percent. It is only when you get up into maximum earners you begin to see a future reduction in benefits.

Senator BREAUX. But their individual accounts would offset that.

Senator KERREY. That is exactly right. It is anticipated their—at that rate, it is anticipated the individual accounts would offset that.

Senator BREAUX. More than offset it.

Mr. McCRERY. What about the KidSave accounts? Are they connected in any way to the Social Security benefits?

Senator BREAUX. I am going to defer to the author of this.

Senator KERREY. Well, the answer is yes. They are not funded with the payroll tax, but the answer is yes, and the idea here is that these accounts need to be opened sooner rather than later, because if you wait and somebody actually goes into the work force, you have given up 14, 15, 16 years of compounding interest rates. So, they are funded with general revenues, but they are part of the personal savings account and run by the Social Security Administration.

Mr. McCRERY. So, there would be a clawback on these, as well?

Senator KERREY. Oh, I see what you are saying, yes, on half of that amount.

Mr. McCRERY. OK, thank you very much, and I commend all of you, particularly my colleague from Louisiana for your courage and your scholarly work on this.

Senator BREAUX. Kamikaze mentality. [Laughter.]

Chairman ARCHER. Mr. Tanner.

Mr. TANNER. Thank you, Mr. Chairman. I will be very brief. I want to also thank you for holding this hearing and also our witnesses. I am encouraged. We have finally gotten people to acknowledge the fact that in reality whatever is or isn't in the Social Secu-

rity lockbox is fairly immaterial, that in 2030 or 2040, we the people are going to owe whoever is alive at that time that's 65 or older whatever benefits the law says they are entitled to receive.

We owe no more and we owe no less. And I think that is fairly—I have heard agreement on that point. So I think we have made some progress this morning.

I want to commend you all for what I think is and has been accorded this plaudit by others, namely the Concord Coalition, as the most fiscally sound approach to fixing this problem. I have been one of the ones as has Charlie Stenholm, who is going to testify in a minute, concerned about the Nation's debt.

There is a debt from the Treasury to the Social SecurityTrust Fund. There is also an outside debt of about $3.5 trillion. The rhetoric around here has been, well, let's take this projected surplus and let's either dump it in the Social Security lockbox, which will create, I suppose, more debt from the Treasury to Social Security. Or, let's take it and cut taxes with it.

There has been very little rhetoric around here about let's take that and redeem that non-Social Security debt of $3.5 trillion, a third of which is owned by other countries, or nationals of other countries.

I say that only to say that in your plan, you financed your changes basically by a carve-out. Is that correct? Is that a fair characterization? A carve-out within the present Social Security tax structure.

Senator KERREY. We make—the principal changes that fund our proposal, that make—and by fund I mean restore the solvency in perpetuity so that you can keep the promise to all 270 million beneficiaries as well as reduce the payroll tax 2 points.

The principal changes are—there is recapturing the honest CPI calculation, where recalculating benefits as life expectancy increases as well as eliminating that hiatus. And we have a number of other proposals that change the benefits in the future that fund the proposal.

Senator BREAUX. The other one that I would mention too is the restoration of the Social Security taxes that are now being shifted off into Medicare, bringing that back into the program as well.

That's the principal way it is funded.

Mr. TANNER. Some of these other programs, the old phrase no pain, no gain comes to mind, and I—you all are to be commended for your courage in saying that in order to make this system better we are going to have to make some structural changes.

Senator BREAUX. Let me just make a comment on that, Mr. Tanner. I think that you are absolutely, and I think the people are ahead of us on this. I think the American people know that this program and Medicare, for example, are in serious problems. And there is no magic wand, and we got to quit saying there is.

And I think people are more realistic about making changes for their children and the grandchildren now then they have ever been before.

Senator KERREY. I also stress the point, Congressman, I made earlier, is that—and that is that in addition to the fork in the road that we take at the beginning, whether or not you want to take action now or postpone it and do it mañana.

The second one is, do you want people in their old-age years to be more dependent or less dependent on the government? And if you want them to be less dependent, then you have to have a mechanism that allows them accumulate wealth over the course of their lifetime.

And there is no question it is possible to do it. And even if you take the most conservative investment, and that is essentially the common ground between what the Chairman has proposed and Congressman Shaw has proposed. I mean, the idea is to increase people's self-sufficiency by giving them their own source of wealth.

Mr. TANNER. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Portman.

Mr. PORTMAN. Thank you, Mr. Chairman. And I want to congratulate the two of you and Senators Gregg and Grassley for cobbling together a bipartisan and, as we will hear in a moment I think, bicameral proposal. I know that is not easy. And that is going to be the only way we are going to be able to move forward.

Senator Kerrey, in your testimony you talked about the individual accounts being the centerpiece of the proposal, and I wanted to follow on with some questions along the lines of Jim McCrery's and commend you for that. I mean, what you have done is you have harnessed the power of compound interest that Senator Gramm focused on in his testimony. But you have also given people independence and dignity and security in retirement, which you focus on.

And that, it seems to me, although not a magic solution, it is about as close as you can come to helping solve this problem without some of the difficult benefit cuts that go beyond those adjustments you make or increasing taxes.

Two percent diverted, and then there is a government match for low-wage workers. You have a Thrift Savings Plan kind of option: government will regulate thus where you can invest. You can't invest in your brother-in-law's real estate venture in Florida. You have got to keep it within the account.

In order to get your SSA actuary, did you have the 60 percent equity investment in that?

Did you make an assumption as to how that would be invested? I notice in your material, you talk about investing in treasuries.

Senator KERREY. No.

Senator BREAUX. No. It is not dependent.

Mr. PORTMAN. OK. You don't need to do that because people keep their accounts. You don't use that necessarily to fund the Social Security system long term?

Senator BREAUX. No.

Mr. PORTMAN. So people would be able to go into treasuries if they chose to?

Senator BREAUX. Yes. Now they would be, Congressman, in the same situation we have and all of us have in our Thrift Savings Plan. I mean, you could put it all in the low-risk, which would probably be government bonds, or you could put in a mixture of the two, or you could put it all in the stock market.

Mr. PORTMAN. That's a significant difference from some of the other plans that have to make certain assumptions in order to

meet the actuarial requirements. People can add up to $2,000 a year. There is no cap on that, on income?

Senator BREAUX. There is none.

Senator KERREY. No. No cap on any——

Mr. PORTMAN. So anybody can put $2,000 a year in, unlike an IRA now, where it is capped.

Senator BREAUX. I mean, you could refine it further. And if someone wanted to refine it, we put caps on it, but we do not.

Senator KERREY. Indeed, I would say in response to that too, I think it is important for me to restate at least, that the savings accounts are a means to an end. And the end is financial security that comes through wealth. And the reason I say that to start is because if you buy into that as the goal, then I think you would want to combine Social Security reform with pension reform and tax reform that currently penalizes all savings.

It seems to me, if you buy into the goal that you want to help that low- or medium-wage individual accumulate wealth over the course of their life and the security that comes with that and decrease dependency on the government in those years, I think you would want to look at doing more than just changing the Social Security system.

Mr. PORTMAN. Thank you for saying that. That way, I don't have to say it with regard to pension reform. And I don't want to bend the Chairman's ear again on that, but I agree with you. And I think this is complementary to the kind of things we are talking about in the pension area, to give people more security through reducing regulation, allowing them to save more. Just letting the government help rather than get in the way.

Two quick questions on the individual accounts. First, on the clawback—and one addition in the account would be the KidSave. That goes into the account as well?

Senator KERREY. Yes.

Mr. PORTMAN. So it is one lump sum of one aggregate account. With KidSave, you have a clawback, but it can't be based on the 3 percent that would otherwise have been in the Social Security fund because this is additional money coming from general revenues. How do you determine what out of KidSave is used for the clawback?

Senator KERREY. Are you looking at staff? You should be. [Laughter.]

Mr. PORTMAN. Senator, as you know, I come from the IRS where sometimes they have the advantage. Anyway, I assume you have some formula you have worked out there.

Senator KERREY. The answer is yes. It is roughly half——

Mr. PORTMAN. My point is, I guess the KidSave doesn't come from Social Security payroll taxes. It really comes out of general revenues.

Senator KERREY. That is correct.

Mr. PORTMAN. And it starts right away. And I understand why you want to do it.

Senator KERREY. That's correct.

Mr. PORTMAN. The second question, if you die prior to taking the benefit, whether you died before your retirement age or if you

choose not to take your Social Security benefit at age 62, if you die after that, what happens to the account?

Senator BREAUX. It is your asset. It is inheritable.

Mr. PORTMAN. So survivor benefit is first taken out?

Senator KERREY. No. The survivor benefit——

Mr. PORTMAN. No. It is yours. Survivor benefit is taken care of through the regular Social Security system?

Senator KERREY. That's correct. There is no reduction in either survivor or disability or the old-age benefit.

Mr. PORTMAN. OK. When you turn 62 and you choose, as most people do now, to take your Social Security, do you get a lump sum of this individual account or do you have to buy an annuity or do a variable annuity or something else?

It is your account, so you just——

Senator BREAUX. It's coming to a theater near you. [Laughter and pause.]

Mr. PORTMAN. I know you know the answer if you just——

Senator KERREY. I used to like you, you know, before you asked me this question I couldn't answer. [Laughter.]

Mr. PORTMAN. No. The question is, if you want at age 62 to take your retirement, as most people do, do you get this individual account as a lump sum. Do you get the total amount you built up over the years, or do you get a monthly payment, having purchased an annuity?

Senator KERREY. I just don't know under the final legislation whether we mandated this be converted into an annuity. I personally would prefer that it not. But I think it needs—the thing that I would object to is a provision that would allow an early withdrawal. It needs to be a part of retirement planning, and I believe—do we require it to be converted into an annuity?

OK. So only up to the poverty level is the requirement that an annuity conversion occur.

Mr. PORTMAN. OK. So up to the poverty level, you would have to purchase an annuity through a government, again, regulated group of companies that offer an annuity?

Senator KERREY. That's correct.

Mr. PORTMAN. But above that amount you can take as a lump sum at age 62.

Senator KERREY. That's correct.

Mr. PORTMAN. So you could use it to buy a boat or do something else.

Senator KERREY. Right. That's correct.

Mr. PORTMAN. OK. Thank you very much. And again, I commend you all for your hard work in moving the ball forward and putting all these people together.

Chairman ARCHER. Are there any other questions?

Gentlemen, thank you.

Senator BREAUX. Thank you, Mr. Chairman.

Senator KERREY. Thank you.

Chairman ARCHER. You make a very constructive contribution to this exercise.

Senator KERREY. It has been a pleasure to be with you.

Chairman ARCHER. Our next witnesses are our two colleagues from the House, Congressman Kolbe and Congressman Stenholm.

Gentlemen, welcome. I assume from the previous testimony that your plan is identical. If not, I would like——

Mr. STENHOLM. No.

Chairman ARCHER. If not, then perhaps you might concentrate on explaining the differences between your plan and the plan that the Senators presented to us.

Congressman Kolbe.

STATEMENT OF HON. JIM KOLBE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. KOLBE. Thank you, Mr. Chairman. We will certainly talk about a few of those differences, but I think it is incumbent upon us to highlight some of the important features of the bill. And this may be the second time at bat with this. But we appreciate very much the opportunity to be here today and your Committee's attention to this.

This is such an important issue, I am really pleased that your Committee is having this hearing and the amount of interest that is in this.

As I think you know, Congressman Stenholm and I have been working together on this issue for some time, and we are delighted that the Committee really recognizes the need for comprehensive Social Security reform.

We think we can do it in this Congress this year. In fact, I think we have to do it this year.

Although the window of opportunity is closing fast, we would suggest that the legislation, though not perfect, can serve as a foundation—that is, the legislation we are proposing—can serve as a foundation document for a bipartisan negotiation. My full statement I would trust, I would ask to be placed in the record. And I will just simply summarize.

Chairman ARCHER. Without objection, the full statement of every witness will be inserted in the record.

Mr. KOLBE. Thank you. I would just like to hit on four specific issues that I think are critical to this debate. One, how our plan, the Kolbe-Stenholm, also Breaux-Gregg-Kerrey plan, reduces Social Security's program cost to a sustainable level.

Second, why the plan is better for women than current Social Security law. Third, the property rights and opportunities for wealth creation that exist under our bill. And, fourth, why a carve-out is necessary.

First, while restoring actuarial balance to the Social Security Trust Fund, that is an important step, it is only one measure of the financial stability of Social Security, of any Social Security reform plan. A truly responsible Social Security plan has to control the costs of the Social Security Program over the long term and address the cash shortfalls that begin in the year 2014.

So if we think the budget caps are tight now, imagine the boondoggle, the budget boondoggle when the growth of Social Security and Medicare Programs forces Congress to cut funding for NIH or Pell grants, Meals on Wheels, other important programs by more than 15 percent.

So we need to act now. In fact, I would point out, Mr. Chairman, that the legislation we passed last week, lockbox legislation, is pre-

cisely the key to this whole thing as to why this is so critical. That legislation says, if we solve Social Security, if we reform Social Security, we have opened the lockbox. That money then becomes available to us for tax relief, for spending that we deem is necessary. And that is why the key to a successful legislative session this year on all the other things that I know our conference and the Minority conference have been focusing on is in getting a reform to Social Security done this year.

According to the actuaries of the Social Security Administration, our plan would restore the costs of the Social Security system to sustainable levels. Now you have in your chart, in your packet a chart that shows—that is hard to see from there, so it is in the packet of information that has been given to you.

The costs under our plan, the cost of the Social Security system will average 14 percent of payroll over the 75-year period compared to 16.4 percent under current law. The cost of the Social Security system under our proposal will never exceed 15.7 percent of payroll. And under current law, those costs of Social Security system would reach 19.6 percent of payroll by 2075 and, from all projections, just continue on growing.

Our proposal and the Senate bipartisan proposal will do more to control the costs of the Social Security system than any other proposal, and that is illustrated by the second table that is in your packet. The average cost rate of your proposal, Mr. Chairman, is 14.6 percent, the maximum rate 17.8. Ours is 14.0; the maximum rate if 15.7, and the others, Gramm is 14.9, the maximum rate 17.6. And we don't have data to analyze the others, the Stark-DeFazio legislation that was introduced fairly recently.

The second point I want to mention is the impact on women. We think it—we know that it will be more beneficial, beneficial to more women than is currently the law. And the main reason for that is the minimum benefit provision that is in our legislation. That, the benefit for 40 years of work equaling 100 percent of poverty, that provision alone mean 50 percent of women would end up with a better payment—we are talking about now the defined payment—better than they have under the current law. And that is before you have any of the other provisions of savings and the other provisions.

We also allow for voluntary contributions, which women could use. They could put an additional $2,000 a year into their personal account. Those that take time off to raise children can catch up by making the contributions later.

And for women who earn under $30,000, ours has a savings subsidy program. For the first dollar voluntary contribution, an eligible worker would receive $150 from the Federal Government. And then each additional dollar is matched 50 percent up to a cap of $600 per year.

This is, in a sense, we have captured this concept from the President's USA savings plans, his proposal.

One of the reasons for the Kolbe-Stenholm bill will be a better deal for women, and this has not been focused on very much, is the changing nature of divorce. Current law stipulates that if a marriage lasts 10 years or more, a woman is entitled to 50 percent of her ex-spouse's Social Security benefit.

Unfortunately, not only has the divorce rate skyrocketed, but the marriages are not lasting as long as they once were. Two or more decades ago, divorces were few and occurred 15 to 20 years after marriage. Today, they are more likely to occur in the fourth to the seventh year of marriage. And more and more women are not remarrying.

So consequently many women are heading into retirement alone without the benefit of a spouse's Social Security income. And what ours does is to supplement that with the provisions that I just mentioned to you.

The third point I'd like to make is about property rights and opportunities for wealth creation. Our legislation establishes the opportunity for all Americans to create wealth and benefit from the power of compound interest.

Several of the people testifying today have, of course, talked about that. The high-income workers have those now with 401(k) plans, Keogh plans, IRA's, mutual funds. We would extend that to moderate, to low- and moderate-income workers. The personal accounts in our plan are wholly the personal property of the worker, in contrast to some of the reform plans. Whether the worker dies before or after drawing on the account, the account remains in their possession and may be bequeathed to their heirs.

Moreover, under our plan, every worker has the right to choose their own risk profile, including the freedom to invest in safe, risk-free treasury securities, just as we do now with the Thrift Savings Plan. As you have that option, that would exist under our plan, which is modeled after the Thrift Savings Plan.

We force no one to invest in the stock market if they choose not do so. The individual accounts in our plan are based on one very simple principle: It is your money, and it ought to be your choice about how you invest it.

Last, let me mention why a carve-out is necessary. It is my fear that policymakers both here and in Congress—both here in Congress and in the White House, believe that reformers will accept personal accounts in any form, including as an add-on to the current system. But I think this is a misjudgment, Mr. Chairman.

I think a carve-out is essential to any fiscally responsible plan that seeks to address the $7.4 trillion unfunded liability in Social Security. Opponents to personal accounts argue the carve-out is destabilizing to Social Security, but that is simply not true.

As long as a carve-out is used to prefund out-year liabilities, a carve-out actually enhances the long-term viability of Social Security by preventing enormous buildup of IOUs in the Social Security Trust Fund. IOUs somehow have to be, eventually, at some point, translated into cash benefits. So we shouldn't fool ourselves. IOUs are merely first claims on future Federal revenues.

Mr. Chairman, you have been very clear in saying that yourself. Voters know that they can fund it only through increased taxes, reducing the benefits, additional debt, redirecting spending from other programs. And under current law, the Social Security Administration estimates that at its peak, the trust fund would contain over $4.4 trillion of IOUs that somehow have to get eventually translated into cash benefits.

So carve-out uses payroll taxes collected today to prepay a portion of retirement income of future retirees rather than leave the entire burden of funding this obligation to our children and grandchildren.

In conclusion, Mr. Chairman, let me say the Congress should not, cannot, should not shirk from its responsibilities in favor of political expediency. We ought to be ashamed if we can't, as a Congress, set aside our political differences to save a program that is as important as Social Security. If we can't do this now, if we can't exert some leadership on this, this year as you have done, Mr. Shaw has done, and others have done, how could we justify asking the voters to return us to office?

Charlie Stenholm and I, along with our colleagues in the Senate plan you just heard about, put together what we believe is the most progressive and the most fiscally responsible—a centrist plan. It is a plan that enjoys broad-based support both on and off the Hill. And as far as I know, is the only plan that has bipartisan sponsorship.

So I challenge the leaders of both political parties, of our political parties, and the President to take the fruits of our effort and begin bipartisan negotiations immediately. Everyday that passes, every month that we delay, we lose credibility and respect in the eyes of the American people.

The heart of America aches, and it aches for leadership that you can provide, Mr. Chairman. And I know you will not disappoint them, and this Congress should not disappoint them.

Thank you.

Chairman ARCHER. Thank you, Congressman Kolbe.

Congressman Stenholm, we will be pleased to receive your comments, your testimony. And as usual, your entire statement in print will be inserted in the record. And you may proceed.

STATEMENT OF HON. CHARLES W. STENHOLM, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. STENHOLM. Thank you, Mr. Chairman, and thank all Members of the Committee for this hearing and for allowing us the privilege of appearing before you.

I want to emphasize two points of the bill that Jim has talked about. One is the fiscal responsibility side of our bill, and two is the strengthening of the safety-net issue.

Just in repeating one thing, this is a bipartisan proposal. I had a goal this year of doubling the number of Democratic cosponsors of our bill. We exceeded that by 100 percent. We have now have three cosponsors on our side instead of just the two, the goal. And we have high hopes.

But it is also bicameral, bipartisan, and I think everyone agrees that if we are going to do that which you, Mr. Chairman, Mr. Shaw and others have suggested doing, it is going to have to be a bipartisan effort and bicameral effort.

And we think we have the broad outline of doing just that. The hallmark of our plan is honestly addressing the financial problems facing Social Security and tackling the tough choices that are necessary.

Restoring solvency is important, but simply restoring solvency over the 75-year period is not enough. Basic questions that need to be asked of any plan. Does the plan put the Social Security system on a permanent, sustainable course that will continue to remain strong at the end of whatever period we choose to use for estimates? Or does it leave the trust fund in a deteriorating condition at the end of the period?

Does the plan deal with the liabilities on general revenues that will put tremendous pressure on the rest of the budget beginning in 2014, as Mr. Shaw emphasized a moment ago? Does the plan control the costs of the Social Security system to ensure that we have the resources to deal with the other priorities of our budgets?

The growth in the cost of the Social Security Program will crowd out other programs. Between now and 2032, the percentage of our national income consumed by Social Security will increase by 50 percent. According to CBO's long-term budget projections, spending on Social Security consumed slightly less than 20 percent of total Federal revenues today. It will grow to 23.5 percent of total revenues by 2015 and nearly 30 percent of total revenues by 2030.

There will be no room in any domestic initiatives. And we will have to cut back on existing programs if we don't take action now. Under the CBO baseline, Social Security will consume an ever-growing portion of the budget.

There is no free lunch. The promised benefits under Social Security will cost $20 trillion more than we can afford over the next 75 years. That money will have to come from somewhere. Now, here, comparing the benefits of any reform plan to the benefits promised under current law, is unfair because current law makes promises we cannot keep.

Plans which suggest we can save Social Security without any tough choices depend on taking funds away from other government priorities in order to provide promised Social Security benefits. Our plan makes some tough choices today that will require some sacrifices.

We can either make some tough choices today to honestly deal with the financial challenges facing Social Security, or we can leave a fiscal time bomb for future generations to deal with. Our plan reduces the liability that Social Security will place on general revenues, reduces the liability between 2014 and 2034 by more than 50 percent, reducing a 7.4 trillion liability by more than 3.8 trillion.

This chart shows you the numbers very dramatically of what our plan does for those liabilities. Reducing these liabilities will preserve the flexibility of the future to deal with other problems in addition to providing Social Security.

The area in red on the chart is money that will be available for other programs, whether it be money for education, agriculture, health care, defense, tax cuts, or any other priorities that we may have in the future.

We are able to reduce these liabilities because we use a portion of current payroll taxes to advance-fund future benefits. Creating individual accounts within the existing payroll taxes is much more responsible from a budgetary perspective than the so-called add-on accounts funded above current payroll taxes.

Funding individual accounts above current payroll taxes will create new general-fund liabilities which will increase our national debt and take resources away from other programs. Our plan doesn't have any of the double counting or cost shifts that some free-lunch plans rely on to make Social Security appear balanced on paper.

Our plan does not rely on projected surpluses. All of the general-revenue transfers in our bill are completely offset by the CPI recapture provision. Our plan works whether or not surpluses actually materialize. Plans which rely on projected surpluses either place the solvency of the Social Security Trust Fund in jeopardy or create problems in the non-Social Security budget if the surpluses are not as large as currently projected.

Now, strengthening the safety net. There has been a lot of rhetoric about how Social Security reform would hurt or could hurt vulnerable populations. We ask you to sincerely look at what our plan actually does. Our plan restores the solvency of the Social Security Trust Fund in a way that not only protects low-income workers from any reduction in guaranteed benefits. It actually strengthens the safety net provided by the Social Security Program.

The benefit changes in our plan primarily affect middle- and upper-income workers who we believe will benefit from the individual accounts. The new minimum benefit provisions will enable Social Security to lift more of the elderly out of poverty than current law.

Fifty percent of women and 10 percent of all men would receive higher guaranteed Social Security benefits as a result of the minimum benefit provision. A low-wage earner defined by the Social Security Administration is a worker with earnings equal to 45 percent of the national average would have a 10-percent increase in guaranteed benefits from our minimum benefit provision.

Any income from individual accounts would be an added bonus above the poverty protection from the minimum benefit for low-income workers. Under our proposal, no individual who works a full career will have to retire in poverty.

Currently, nearly 8 million seniors receive benefits that are less than the poverty level. We say to all Americans, if you work all of your life and play by the rules, you will not retire into poverty.

We also incorporate the concept from the President's USA proposal of helping low-income workers to save for their retirement by providing subsidies for workers who make voluntary contributions to their individual accounts. The subsidy for low-income workers will increase the retirement income of workers earning less than $30,000 and encourage increased savings among income groups who have very little savings today.

Mr. Chairman, in conclusion, let me say, members on both sides of the aisle can pick out individual items in the plan to criticize us because we didn't go far enough in one area or we went too far in another. We acknowledge that. All we ask is that you look at the entire package and judge the entire plan on its merits instead of picking out individual provisions.

We have never claimed our plan is perfect. We recognize that there may be places where our bill can be improved. We are willing

to work with anyone who has constructive suggestions so long as they are willing to be fiscally responsible.

As we tackle the tough choices that will be necessary to enact credible Social Security reforms, we must look beyond current polls and think about how our children will look back at the decision we make today.

Now there are many that have asked why Charlie Stenholm from the House Agriculture Committee, not normally would be associated with Social Security, how and why I have been as active and why I have been as privileged and pleased to have worked with Jim Kolbe over the last three or 4 years and coming to this point. Well I have two reasons, Mr. Chairman, for being as active as I am in this question and in urging this Committee to act this year.

And their names are Chase and Cole, Cindy's and my 3½-year-old and 1½-year-old grandsons. I have resolved that I do not wish them to look back 65 years from today and say, if only my granddad would have done what in his heart he knew he should have done when he was in the Congress, we wouldn't be in the mess we are in today.

And everyone of us knows in our hearts that unless we act sooner not later, our grandchildren will look back 65 years from today and say that what we should have done.

And that is why we are here, and why again I commend you, Mr. Chairman, Mr. Shaw, Mr. Rangel and others for bringing this to this point and look forward to rolling up our sleeves and working with this Committee in a bipartisan way in order to bring about a solution this year, 1999.

Chairman ARCHER. Thank you, Mr. Stenholm.

[The prepared statement and attachments follow:]

Joint Statement of Hon. Jim Kolbe, a Representative in Congress from the State of Arizona; and Hon. Charles W. Stenholm, a Representative in Congress from the State of Texas

Chairman Archer, Congressman Rangel and Members of the Ways and Means Committee, we appreciate the opportunity to appear here today to discuss Social Security reform and present our legislation for your consideration. We've spent several years working together on this issue and we are delighted that the Committee recognizes the need to address the financial and demographics problems that threaten our nation's most successful anti-poverty program.

In particular, we commend Chairman Archer for setting the bar for this debate at 75-year solvency. Groups on and off the Hill have suggested that this goal may be too ambitious, and that incremental reform may be a better solution. We disagree. It is for good reason current law mandates that the Social Security Trustees evaluate the health of the Trust Fund over a 75-year horizon. This period encompasses the entire future life span of all current workers and beneficiaries, including newborn babies—the beneficiaries of tomorrow. Also, the projection period is sufficient to evaluate the full effect of changes to the Social Security program.

In fact, we would like to see the committee set the bar even higher. We believe the Members should also consider the impact of reform proposals on the annual operating cash flow of the federal government, and on the Trust Fund balance at the end of the 75-year forecast horizon. Solvency alone is an incomplete standard for determining whether legislation truly strengthens Social Security. Solvency is not sufficient if we leave the Social Security system in a deteriorating condition at the end of the period, or if the federal budget incurs massive cash deficits in the interim years.

The difference between a plan that leaves in place a strong and growing Trust Fund at the end of seventy-five years, and a plan that extends solvency for a finite period of time but leaves the system with a depleted Trust Fund, is fundamental and significant. The issue should not be fifty years versus seventy five years, it

should be whether a reform plan offers a complete solution that puts the Social Security system on a permanent, sustainable fiscal course.

A "partial" solution will only exacerbate the cynicism among young people that Social Security won't be there for them. A "partial" solution will require continuous "tinkering" and adjustment, impeding the ability of Americans to plan for retirement with a degree of certainty. Any credible reform plan must put the Trust Fund on a permanent, sustainable fiscal path that will ensure the system remains fiscally sound throughout the valuation period and beyond. Genuine solvency is achieved only if the cash flow is balanced, and the Trust Fund is stable and getting stronger at the end of the forecast period.

We Were Country When Country Wasn't Cool

To paraphrase the country and western song, we were Social Security reformers before Social Security reform was cool. Three years ago, we came together to form the Public Pension Reform Caucus and begin a discussion in Congress. Today, the PPRC has a bipartisan membership of 75 members. Our goal was to educate ourselves and our colleagues about the issues and challenges facing Social Security. Perhaps just as importantly, we sought to demonstrate the type of centrist, bipartisan approach to the substance and politics of Social Security reform necessary to resolve the impending crisis..

Two years ago, we joined Senators Judd Gregg and John Breaux to serve as Congressional co-chairmen of the CSIS National Commission on Retirement Policy (NCRP). The NCRP was a 24-member commission comprised of leaders from the business community and experts on retirement policy. Our goal was to develop a plan to strengthen America's retirement programs, including employer-provided pensions, personal savings and, finally, Social Security. Fifteen months after the panel's creation, we disproved the notion that all commissions must end in disagreement or irrelevance. In a unanimous vote, our commission agreed on the 21st Century Retirement Security Act.

We introduced legislation last Congress (HR 4824, 105th Congress) based on the NCRP report. That legislation generated considerable interest and praise for representing a fiscally responsible approach to strengthen the Social Security program. Since then, we have talked with many of our colleagues on both sides of the aisle, met with Administration's staff to discuss our proposal and listened to constructive criticisms of our plan. The legislation we bring before you today is a revised version of the NCRP plan—a "new and improved" plan that we believe addresses many of the concerns that have been brought to our attention over the last year.

HR 1793: The 21st Century Retirement Security Act

We still adhere to the same guiding principles as our previous legislation: a balanced, actuarially sound plan that reduces the $7.4 trillion unfunded liability, improves rates of return and strengthens the safety net. We accomplish this by using personal accounts to advance-fund future obligations and by implementing much needed structural reforms. We've softened some of the tough choices in last year's bill and included some new provisions aimed at improving the retirement income of the working poor. What we *don't* do, however, is rely on double counting, cost-shifting, uncertain budget surpluses and accounting gimmickry to hide the true costs of reform—unlike some "free lunch" plans that have been offered by the right and left.

Our legislation, The 21st Century Retirement Security Act, provides a payroll tax cut for all working individuals under the age of 55 by diverting two percent of FICA taxes into personal Individual Security Accounts. Workers also would be allowed to make additional voluntary contributions of up to $2,000 a year to their individual account. The legislation also provides a savings match for voluntary contributions to help low-income workers build their individual accounts.

The individual accounts in our plan would be modeled on the federal government's Thrift Savings Plan. In the TSP, individuals personally choose investment options, including a stock index fund, a bond index fund and a Treasury securities index fund. Unlike other proposals, our plan would provide individuals with ownership and control over their retirement assets, including the freedom to invest in safe, risk-free Treasury securities. We don't force anyone to invest their Social Security monies in the stock market—it's your money, your choice.

Our bill also strengthens traditional Social Security's safety net by creating a more substantial guaranteed minimum benefit that ensures stronger poverty protections than currently provided for low-income workers. Moreover, this benefit is given regardless of any other factors. Consequently, any income from the individual ac-

counts would supplement the enhanced guaranteed Social Security benefit for low-income workers.

Our plan makes changes in the defined benefit program, but in a progressive manner that insulates vulnerable populations. Changes to the defined benefit largely affect mid-to-high income individuals who will benefit disproportionately from the individual accounts. We implement additional reforms that reduce the cost of the Social Security program. For example, our plan makes changes to reflect the increases in life expectancy and longer working lives, provides for a more accurate inflation adjustment, and rewards work. While these provisions involve some pain, it is necessary to make tough choices to ensure that future governments will have resources to deal with other problems in addition to Social Security.

We have never claimed that our plan is perfect. Every one of you could go through our plan and select individual items in the plan to criticize—either we went too far or not far enough. We remain open to constructive suggestions about how our plan can be improved. However, we encourage you to look at the plan "holistically"—to examine what the proposal accomplishes in it's entirety, rahter than focus on one or two provisions. If everyone determines the acceptibility or unacceptability of various proposals based ona single element, we'll never achieve the bipartisan consensus necessary to pass a bill and save Social Security.

Kolbe-Stenholm is a Foundation Plan

We respectfully suggest to this committee that the bipartisan work embodied by this legislation offers a foundation for you to commence negotiations and create meaningful, comprehensive reform that can be *enacted in to law this year*. There are several elements in our proposal that we believe are essential to reaching a bipartisan consensus on Social Security reform:

1) Bipartisan. Our proposal is a truly bipartisan solution that balances the objectives of different political perspectives.

2) Solvent. The legislation we introduced has been scored by the actuaries of the Social Security Administration as restoring solvency to the Social Security program for the next seventy five years and beyond.

3) Fiscally responsible. Our legislation tackles the tough choices that are necessary to control cost and reduce the pressures on future general revenues. It does not use cost shifts or other accounting gimmickry and does not rely on projected surpluses to create new general fund liabilities.

4) Empowers all Americans. The legislation establishes individual accounts that provide *all* Americans the opportunity to create wealth, and provides individuals with ownership of and control over their retirement assets.

5) Enhances the safety net. Our legislation contains several provisions in both the defined benefit program and individual accounts that provide stronger poverty protections and greater assistance to low-income workers than are contained in current law.

6) Rewards work. The legislation makes several reforms to enhance the work incentives in the current system.

7) Improves Social Security for all Americans. Our proposal provides all future retirees with a better rate of return than the current system can afford, and protects all taxpayers from the increased tax burden created by the existing general fund obligations to the Social Security system.

The Kolbe-Stenholm Plan is Bipartisan

An agreement on legislation to strengthen Social Security will require bipartisan cooperation. We must put party affiliations aside and think about the future generations who will be affected by the decisions we make today.

The Kolbe-Stenholm plan is a model for building this bridge. The Social Security reform debate has been characterized as an either-or choice between two ideological poles—"status" or "full privatization." Defenders of the status quo argue that any reform that includes a market-based component will undermine the current safety net features and expose workers to dangerous risks. Advocates of full privatization suggest that the creation of privately managed personal accounts will painlessly solve every challenge while, in fact, they ignore existing long-term liabilities and the needs of special populations. Both extremes make for good, albeit myopic, rhetoric and fail to acknowledge the virtue of hybridization. The complete solution to the Social Security problem can and must combine the best of the traditional program with new market-based options.

Our plan attempts to balance three competing objectives we think are necessary to achieve a responsible consensus that can win the support of the left, right and middle of the Social Security debate. It establishes individual accounts to improve

rates of return for all retirees—the key objective of most Republicans. At the same time, it maintains and strengthens the important protections that the Social Security system provides for low-income retirees, survivors and the disabled—the key objective of most Democrats. Last, but definitely not least, it honestly deals with the financial challenges of Social Security, the key concern of those of us in the radical center.

THE KOLBE-STENHOLM PLAN IS FISCALLY RESPONSIBLE—OR "SHOW ME THE MONEY!"

Our plan sets the standard for a credible, responsible solution to Social Security. The 21st Century Retirement Act ensures the Social Security program will operate on a solid, sustainable fiscal path well into the next millennium. It does this by honestly and responsibly addressing the unfunded liabilities of the program.

Three distinguishing characteristics separate this plan from other prominent proposals. First, unlike the President's proposal, our plan restores the Social Security Trust Fund to 75-year actuarial balance. Second, unlike several "free lunch" proposals, our plan addresses the cash deficits that begin in 2014 (when benefit costs exceed payroll tax revenues), by reducing the pressure on general revenues and preserving the flexibility of future governments to meet other critical budget needs. Third, the 21st Century Retirement Security Act does not depend on projected budget surpluses, cost shifts or accounting gimmicks to balance the Social Security program.

The 21st Century Retirement Security Act restores solvency of the Social Security Trust Fund by eliminating the entire projected cash shortfall in the Trust Fund over the next 75 years. Moreover, it does so using conservative economic assumptions. Just as importantly, the 21st Century Retirement Security Act makes structural reforms to the Social Security system that help restore the traditional program to a path of long-term solvency that does not deteriorate over time. The Kolbe-Stenholm plan puts Social Security revenues and outlays on a sustainable course over the entire 75-year period. The Trust Fund ratio—the amount of cash reserves in the Trust Fund relative to projected benefits—is rising at the end of the 75-year period. Thus, there is no "cliff effect."

While restoring actuarial balance to the Social Security Trust Fund is an important step, it is only one measure of the financial stability of a Social Security reform plan. A truly responsible Social Security plan must control the costs of the Social Security program over the long term and address the cash shortfalls that will create tremendous liabilities on general revenues beginning in 2014. Controlling the costs of the Social Security system is essential to the fiscal health of our government. If we do not address the pressures on the rest of the budget caused by the growth in the costs of Social Security, future Congresses will be forced to cut other important government programs or raise additional taxes to meet the obligations to our senior citizens. Not only will there be no room for any domestic initiatives; we will have to cut back on existing programs to make room for growth in spending on Social Security

According to the Congressional Budget Office long-term budget projections, which assume that we will use 100% of projected surpluses to reduce our national debt, Social Security will consume an ever growing portion of the federal budget, creating tremendous budgetary pressures. Between now and 2030, the percentage of our national income consumed by Social Security will increase by 50%. Spending on Social Security consumes slightly less than 20% of total federal revenues today. CBO projects that Social Security will grow to 23.5% of total revenues by 2015 and nearly 30% of total revenues by 2030.

The tough choices we struggle with in the current appropriations cycle are mild compared to the problems we will leave for future Congresses if we do not take action now to control the costs of the Social Security program. By 2025, spending on programs other than Social Security and Medicare will have to be reduced by nearly 9% below current levels if we do not take action. By 2030, spending on programs other than Social Security and Medicare will have to be reduced by 16% below current levels.

Under current law, the U.S. Treasury must find $7.4 trillion in cash from general revenues between 2014 and 2034 to convert the IOUs in the Social Security Trust Fund into cash benefits for Social Security recipients. These general fund liabilities will be more than $200 billion a year by 2020 and more than $800 billion in 2030 alone. After adjusting for inflation, the amount of general revenues that will need to be provided to the Social Security system in 2030 to provide promised benefits will be greater than total non-defense discretionary spending last year.

The 21st Century Retirement Security Act restores the costs of the Social Security system to sustainable levels. According the Social Security Administration actuaries,

the costs of the Social Security system will average 14.0% of payroll over the 75-year period under our plan, compared to 16.4% under current law. The costs of the Social Security system will never exceed 15.7% of payroll under our plan. Under current law, the costs of the Social Security system will reach 19.6% of payroll by 2075 and will continue growing. Our proposal and the Senate bipartisan proposal will do more to control the costs of the Social Security system than any other proposal. In fact, several prominent proposals that have been put forward would actually result in higher costs for the Social Security system than the projected costs under current law (see Table 1).[1]

Table 1. Comparison of Cost Rates of Current Law and Alternative Plans

(as a percent of Taxable Payroll)

Year	Current Law	Archer-Shaw	Senate Bipartisan	Kolbe-Stenholm	Gramm	Nadler
2000	10.8	12.8	12.7	12.9	15.0	
2005	11.2	13.3	13.2	13.0	15.2	
2010	11.9	13.9	13.4	13.4	15.6	
2015	13.3	15.0	14.0	14.0	16.4	
2015	13.3	15.0	14.0	14.0	16.4	
2020	15.0	16.4	14.7	14.8	17.3	
2025	16.6	17.4	15.4	15.6	17.6	
2030	17.7	17.8	15.7	15.7	17.1	
2030	17.7	17.8	15.7	15.7	17.1	
2030	17.7	17.8	15.7	15.7	17.1	
2035	18.2	17.3	15.5	15.2	16.4	
2040	18.2	16.2	14.8	14.5	15.2	
2045	18.2	14.9	14.3	13.8	14.1	
2050	18.3	13.8	13.9	13.3	13.4	
2055	18.6	13.1	13.7	13.2	13.0	
2060	19.1	12.6	13.7	13.2	12.8	
2065	19.4	12.3	13.6	13.4	12.5	
2070	19.6	12.1	13.5	13.7	12.4	
Min	10.8	12.1	12.7	12.9	12.4	NA
Max	19.6	17.8	15.7	15.7	17.6	NA
Avg	16.4	14.6	14.1	14.0	14.9	NA

Because our plan advance-funds future liabilities and addresses tough choices, it will dramatically reduce the general fund liabilities that exist under current law. By contrast, the leading plans proposed from the left and the right leave this liability in place and actually increase these general fund liabilities for the next fifty years. According to estimates prepared by the Social Security administration actuaries, the 21st Century Retirement Security Act would reduce the $7.4 trillion liability facing general revenues between 2014 and 2034 by approximately $3.8 trillion, a reduction of more than 50%. It would reduce the amount that the federal government will have to come up with from general revenues in 2025 from $420 billion to $217 billion. In 2030, our plan would reduce the burden on general revenues by more than half a trillion dollars, reducing a $814 billion liability to just $272 billion.

These reductions represent resources that will be available for other priorities, including programs for education, training, health care, debt reduction or tax cuts. The tough choices that are contained in our plan to control program costs must be viewed in context of the resources that would be freed for other priorities. Likewise, any evaluation of "free lunch" plans that claim to save Social Security without tackling tough choices must consider the problems these plans shunt onto the rest of the budget—problems that will be left for future Congresses. We can responsibly tackle some tough choices today or we can leave a fiscal time bomb for future generations. A plan that restores the Social Security Trust Fund to 75-year actuarial balance, but does not address the budgetary pressures created by these growing costs and general fund liabilities, does no favors for future generations.

Unlike other Social Security reform plans that are dependent upon funding from projected surpluses, the 21st Century Retirement Security Act is entirely self-financed and will achieve its goals whether or not current surplus projections are ac-

[1] Source: Office of the Actury, Social Security Administration. Archer-Shaw plan memo dated April 29, 1999; Senate Bipartisan plan memo dated June 3, 1999; Kolbe-Stenholm plan memo dated May 25, 1999; and Gramm plan memo dated April 16, 1999. Nadler plan memo unavailable on date of publication.

curate. Although our plan relies on general revenue transfers, all of the general revenue transfers in our plan are paid for by savings in the non-Social Security budget from the CPI recapture provision. Plans which rely on general revenue transfers financed by projected surpluses either place the solvency of the Social Security Trust Fund in jeopardy, or create problems in the non-Social Security budget if the surpluses are not as large as currently projected. Under our plan, if the surpluses do materialize, they would remain available for debt reduction, strengthening Medicare, tax cuts, or spending on other priorities.

The 21st Century Retirement Security Act does not rely on double-counting, optimistic assumptions or other gimmicks to make the plan appear balanced on paper. The plan does not mask the costs of the program by shifting costs to other areas of the budget or the private economy. All payroll taxes are used only once, either to fund current benefits, fund individual accounts, or credit the Trust Fund. Unlike other plans, the Kolbe-Stenholm plan does not use Social Security surpluses already credited to the Social Security Trust Fund to justify a second round of credits to the Trust Fund. Nor does the plan pay for individual accounts with funds that already have been credited to the Trust Fund, like some "free lunch" plans do.

We learned a long time ago that if something sounds too good to be true, it probably is. There is no free lunch. We cannot afford to meet all of the promises in current law without finding additional resources elsewhere. Proponents of plans that claim to preserve benefits at levels promised under current law, or even suggest that benefits will be increased above current law, must answer the call "Show me the money!" Where does the money come from to fund these promises? These so-called "free lunch" plans which suggest it is possible to save Social Security without any pain actually have tremendous hidden costs that will require very real pain. They will drain the federal budget and U.S. economy of resources that are needed for other government programs. They will result in higher tax burdens and lower national savings. Congress and the President must honestly address the fiscal challenges posed by the Social Security system, instead of ignoring hidden costs and pretending that we can meet these challenges without tough choices.

H.R. 1793 Empowers All Americans with Freedom and Control over their Retirement Assets

H.R. 1793 creates individual accounts based on the federal employees' Thrift Savings Plan. This model combines the benefits of individual ownership with the protections offered by a quasi-private board governing fund managers. The TSP model offers a straight-forward, low-cost retirement savings mechanism safeguarded against fraud and abuse. The Thrift Savings Plan has been an extremely successful program for all federal employees, including Members of Congress. The burden of recordkeeping for each individual account would be assumed by the Board. Employer burdens and administrative costs would be kept to a minimum. The administrative costs would be spread across accounts proportionally based on account balances to limit the impact of administrative charges on small accounts.

Under our legislation, every worker would be able to choose from among a number of investment options selected by a quasi-private Board based on a competitive bidding process. Workers would have the opportunity to choose between options with higher risk and the potential of a commensurate higher return and those that are safer, with lower rates of return. The options would include a stock index fund, a bond index fund, and a government securities fund. No worker would be forced to put his or her retirement funds in the stock market. Workers would have the opportunity to select their own risk profile, including the freedom to invest in safe, risk free Treasury securities. Conversely, workers who want to take advantage of stock market returns could place all or most of their account in stock funds. The individual accounts under our plan are based on a simple philosophy: it's your money, your choice.

Opponents of individual accounts highlight examples of poorly implemented individual account systems in other countries that resulted in high administrative costs. There are legitimate administrative cost concerns about purely privatized individual account plans involving dozens of private account managers. However, these concerns can be addressed without eliminating individual control and turning investment decisions over to the government. Our legislation demonstrates that it is possible to give individuals control over their retirement income while also providing government safeguards that address legitimate risk concerns.

Federal Reserve Board Chairman Alan Greenspan and others have made a persuasive case about the risks of social investing, government interference in the market and conflicts of interest inherent in having the Trust Fund invested by the government in the stock market. Most significantly, though, the collective investment

approach doesn't address the central impetus behind calls for individual accounts: taxpayers want their own stake in the economy and more control over their retirement benefits.

Critics argue that individual accounts are too risky for lower-income individuals. We believe that it is more risky, and certainly unfair, not to give lower-income individuals the opportunity to realize the benefits of accumulating assets. It is precisely this lack of investment opportunity that has left too many Americans on the fringe of the economy. Our legislation gives low-income workers the same opportunities to have savings for their retirement and reap the benefits of investment earnings that are already available to higher earning workers who benefit from 401(k) plans and other private savings vehicles. For low-income people, the individual security accounts are a pure bonus above and beyond the strengthened safety net provided by the guaranteed minimum benefit provision included in our legislation.

Why a Carve-Out is Necessary

H.R. 1793 creates individual accounts within the existing payroll tax structure instead of creating individual accounts above the current 12.4% payroll taxes. Some plans "add on" personal accounts through explicit or implicit tax increases or by diverting revenues from other programs. Diverting a portion of payroll taxes to create individual accounts—sometimes referred to as a "carve-out"—has been criticized as weakening the financial status of the Social Security system and requiring deeper benefit cuts than otherwise would be necessary. This argument completely ignores the benefits of using individual accounts funded with current payroll taxes to replace a portion of future unfunded liabilities instead of building up Trust Fund assets.

By placing a portion of current payroll taxes into individual accounts that will be available to provide retirement income for future retirees, our legislation would significantly reduce future unfunded benefit promises without reducing retirement income for these retirees. Under our plan, a portion of retirement income for future retirees will come from payroll taxes collected today and placed in individual accounts, instead of leaving the entire burden of funding retirement income to future taxpayers. The reductions in future liabilities on general revenues that we outlined earlier in our statement are possible because of the prefunding through individual accounts created with existing payroll taxes.

While there has been a lot of discussion about the transition costs of creating individual accounts, the transition costs resulting from advance funding future benefits must be viewed in context of the reductions in future liabilities that are achieved by this advance funding. Proposals which rely on increasing the balances of the Social Security trust fund to meet future benefit promises instead of creating individual accounts effectively leave the financial burden of providing retirement income for future retirees to future taxpayers. The transition costs of creating individual accounts out of existing payroll taxes are much smaller than the liabilities that future taxpayers will face in redeeming trust fund balances under current law. Those who criticize plans to advance fund future benefits with individual accounts because of the transition costs resulting from diverting a portion of current payroll taxes should be asked to explain how they plan to meet the general fund liabilities that would be reduced under our plan. Our legislation takes responsibility for itself and preserves the flexibility of future Americans to address other national needs.

There have been some suggestions that creating individual accounts outside of the existing payroll taxes—sometimes referred to as an "add-on"—would represent a compromise on the issue of individual accounts. We strongly disagree with that suggestion. In fact, creating individual accounts above the existing payroll tax would actually exacerbate the concerns that we have outlined about the budgetary pressures that will be created by retirement programs under current law. That would represent a major step backwards from current law, not a compromise.

Since there is very little willingness to explicitly require additional contributions above the current 12.4% payroll tax rate to fund individual accounts, most proposals that create individual accounts outside of the current payroll tax are funded with general revenues from projected surpluses. This approach presents some very serious problems in terms of fiscal responsibility, future tax burdens and resources available for other needs. Even if projected surpluses materialize as currently estimated—an uncertain prospect at best—they will not last indefinitely. However, the obligation to fund individual accounts from general revenues would be permanent.

A Congressional Budget Office analysis of one such plan to create individual accounts with general revenues warned that this approach would result in higher implicit tax burdens, increased budgetary pressures and a higher national debt. The Social Security Actuaries have found that creating individual accounts of 2% funded

with general revenues could increase the national debt by more than $10 trillion above current projections over the next thirty years. Creating individual accounts outside of the existing 12.4% payroll tax means higher tax burdens on future generations, less resources available for all other government priorities, and higher debt. We cannot afford to ignore the very serious fiscal consequences that this approach would have in the future in order to meet political needs of today.

The real question isn't whether or not a plan has individual accounts, it is whether the plan uses the individual accounts to address future liabilities to taxpayers. Unlike plans which use current payroll taxes to prefund future benefits instead of building IOUs in the Trust Fund, individual accounts funded outside of the current payroll tax would allow the Trust Fund to continue to accumulate IOUs. These IOUs are merely claims against future general revenues. Using current payroll taxes to create individual accounts and advance fund future benefits will substantially reduce the liabilities on future general revenues. By contrast, individual accounts added on top of the current system take funds from general revenues today and leave in place the future liabilities on general revenues. This is a fundamental difference from a fiscal perspective that must not be brushed aside to reach a political compromise.

The Kolbe-Stenholm Plan Strengthens the Government Safety Net

The 21st Century Retirement Security Act restores the solvency of the Social Security Trust Fund in a way that not only protects low-income workers from any reduction in benefits, it actually strengthens the safety net provided by the Social Security program. It contains a new minimum benefit provision that offers stronger poverty protection than provided under current law. The plan also provides a subsidy to supplement the individual accounts of low-income workers. Finally, by addressing the unfunded liabilities of the Social Security without shifting new obligations onto general revenues, our plan reduces the pressure to cut funding for other government programs that benefit low-income populations.

One of the innovative features of our bill is a minimum benefit provision that provides a much stronger safety net for low and moderate-income workers when they retire than is contained in current law. An individual who has worked for 40 years and qualified for 40 years of coverage will be guaranteed a Social Security benefit equal to 100% of the poverty level. Workers would be eligible for a minimum benefit equal to 60% of poverty after 20 years of work, and the minimum benefit would increase by 2% of the poverty level for each additional year of work. This minimum benefit level is calculated without regard to any other change in the benefit formula under our legislation. Any income from the individual accounts would supplement this guaranteed benefit. Widows would be covered by the minimum benefit guarantee based on his or her spouse's work history.

The new minimum benefit provision will enable Social Security to lift more of the elderly out of poverty than current law. Currently, nearly 8 million seniors receive benefits that are less than the poverty level. According to the Social Security Administration actuaries, 50% of women and 10% of men would receive higher guaranteed Social Security benefits as a result of the minimum benefit provision in H.R. 1793. For a low-wage worker, defined by the Social Security Administration as a worker with lifetime earnings equal to 45% of the national median, the minimum benefit provision increases retirement income by more than 10% (see Table 2)—not including any balances that would accrue in the worker's personal account. We say to all Americans—if you work all your life and play by the rules, you won't retire into poverty.

Table 2. Impact of the Minimum Benefit Provision on a Low Wage Worker

Low wage worker earning 45% of the National Average Wage ..	....	$12,600 / yr
Current Law Social Security benefit.		
Social Security Benefit at Normal Retirement Age:	$568	
Plus: Spousal Benefit (if applicable):	$284	
Equals: Total Monthly Social Security Benefit:	$852	
Social Security Benefit under Kolbe-Stenholm.		
Poverty Level for a single-person household over age 65	....	$7,525
Translated into a monthly benefit (divide by 12)	$627	
Plus: Spousal Benefit (if applicable)	$314	
Equals: Total Monthly Social Security benefit	$941	
Note: this amount does not include any balances that accrue in the workers personal account. Consequently, total benefits will be higher.		
Kolbe-Stenholm increase over current law benefits:	$89 /month 10.4%	

The Kolbe-Stenholm plan also incorporates the concept from the President's USA proposal of helping low-income workers save for their retirement by providing subsidies for workers. The individual accounts in the 21st Century Retirement Security Act will give low and moderate income workers the opportunity to benefit from investment opportunities that higher income workers already have with 401(k) plans, IRAs and mutual funds. To help low-income workers take advantage of this new savings vehicle the Kolbe-Stenholm plan provides a savings subsidy, or "match" for low-income workers who make voluntary contributions to their individual account. A maximum of $600 per individual is allowed per year. To qualify for the subsidy in any given year, an individual must earn less than $30,000 per year and make at least $1 in voluntary contributions to their personal account. The subsidy for low income workers will help increase retirement savings for lower income workers who do not have access to private pensions and have little or no other savings for retirement.

We've discussed in detail the reduction in the unfunded liabilities of the Social Security system under our proposal. This effect is substantial for low-income individuals as well, because the budgetary pressures that will occur under current law threaten deep cuts in other safety net programs that benefit low-income populations. By honestly addressing the budgetary pressures created by the unfunded liabilities of the Social Security system, our plan ensures that future governments will have resources available to preserve funding for discretionary spending and other programs that benefit low-income families in addition to providing Social Security benefits.

Instead of focusing on rhetoric about what Social Security reform *could do* to vulnerable populations, we encourage you to look closely at what our plan *actually does*. The 21st Century Retirement Security Act demonstrates that a fiscally responsible plan to strengthen the Social Security system and create individual accounts with existing payroll taxes can actually preserve and strengthen the safety net provided by Social Security.

The Kolbe-Stenholm Plan Increases National Savings

It is a basic rule of economics that increasing national savings is vital to maintaining a strong and growing economy. Comprehensive Social Security reform, done properly, could be the most significant action the government could take to increase national savings. Estelle James, a World Bank Economist who has studied retirement systems and across the world and served on the NCRP, wrote in a study of public pension reforms around the world that:

> "... a change from the old traditional pay-as-you-go, defined-benefit type of social security system to a system that includes more funding, more individual accounts, and a closer link between benefits and contributions is good for the overall economy...It helps all countries develop their long-term saving, which seems to be linked to economic growth."

The 21st Century Retirement Security Act contains several features that will help increase national savings. By advance funding a portion of future benefits and tackling the tough choices necessary to control the cots of the Social Security system, our plan dramatically reduces the unfunded liabilities that will place a tremendous drain on national savings in the future. The individual accounts in our plan create a new vehicle for increased retirement savings by allowing workers to make voluntary contributions of up to $2000 a year to their individual accounts. The savings match for low-income workers will provide low-income workers with an incentive and assistance to save for their own retirement. The reductions in the defined benefits for the middle and upper income workers who have the means to save for their own retirement will encourage these workers to increase their private retirement savings. The Congressional Budget Office and several economic studies have found that the existence of high guaranteed benefit levels for higher income workers has the effect of reducing private savings among these workers.

The Kolbe-Stenholm Plan is a Better Deal for All Americans

When all of the provisions of the 21st Century Retirement Security Act are taken into consideration, it offers a much better deal for all Americans than current law. Our plan will put into place a Social Security system that will remain financially strong for the next 75 years and beyond, and reduces the tax burdens that will be necessary to support the system. At the same time, the legislation we have introduced will provide a better rate of return than can be provided under current law and strengthens the safety net for low-income workers. The individual accounts in our plan will allow all workers to create wealth and benefit from market forces. Perhaps most importantly, our plan will help restore public confidence in the future of the Social Security system.

Our legislation increases the rate of return for all workers compared to what current law can fund. Comparing the benefits under our plan to the benefits promised under current law is extremely misleading, because we cannot afford the benefits promised under current law. Today, the Social Security system faces a funding gap that must be closed if beneficiaries are to be protected. Eliminating the funding shortfall under current law through a traditional package of benefit reductions or tax increases would exacerbate the bad deal that Americans receive from Social Security.

Under current law, benefits will have to be cut by more than 25 percent after 2034 unless we raise payroll taxes. If the burden of closing this funding gap were spread evenly among all generations, benefit levels would be cut by nearly 16% beginning immediately. To accurately compare our plan to the benefits promised under current law, it is necessary to consider the substantially higher tax burdens that will be necessary to fund the benefits promised under current law. To the extent that current law promises higher benefit levels than our plan can deliver for some middle and upper income retirees, it can only meet those promises by imposing much higher taxes on those workers. When the benefits promised under current law are viewed in context of the taxes that must be raised to fund those benefit promises, the deal offered by current law is not nearly as attractive for today's workers. When all of the benefits under 21st Century Retirement Security Act are compared to what current law can actually deliver, future retirees will get a much better deal under our legislation than they would under current law.

Our legislation establishes the opportunity for *all* Americans to create wealth and benefit from the market forces to increase their retirement income. Individual accounts will extend to low and moderate income workers the investment opportunities that higher income workers with 401(k) plans and mutual funds already enjoy. Unlike the current system and some other individual account plans, H.R. 1793 will provide individuals with ownership of and control over their retirement assets.

Finally, The 21st Century Retirement Security Act will improve public confidence in the future of the Social Security system. The Social Security system has a well-deserved reputation as one of the most successful government programs in history, and has enjoyed strong public support. However, the financial problems facing the system and the low-rate of return that current workers can expect to receive on their payroll taxes threatens to undermine this support. The plan we have introduced offers a message of reassurance to seniors and a message of hope to younger generations.

Our plan reassures seniors that the long-term challenges facing Social Security can be addressed without threatening the benefits they have been promised. Our bill restores the solvency of the Social Security system while preserving existing benefit promises for current and near-retirees. Current retirees would continue to receive their existing benefits, with full increases for inflation, accurately measured.

By putting the Social Security system on a sustainable fiscal path, our plan protects current retirees from the threat of benefit changes that may be necessary if the Social Security system continues to face financial problems.

While it is important that Social Security reform protect the interests of current retirees, it is just as important that we address the concerns of younger generations that doubt that the Social Security system will be there for them. The Social Security system has always been based on an implicit generational contract that workers will pay taxes to fund benefits for current retirees in the expectation that they will receive similar benefits when they retire. This generational contract is threatened by the growing skepticism among younger workers about the future of the Social Security system. Requiring workers to pay taxes to support a system that they do not expect to benefit from will create discord that can only jeopardize the political legitimacy of the Social Security program.

The 21st Century Retirement Security Act will give younger generations much greater confidence in the Social Security system. Our plan reassures younger generations that the Social Security program will be there for them when they retire by putting the system on a long-term, sustainable fiscal path. In addition, our legislation will give younger workers ownership of and control over a portion of their retirement income, providing them with concrete assurance that the Social Security system will provide them with retirement income. Our legislation will modernize the Social Security system to ensure that it can earn the support of younger generations that will be necessary to preserve the program.

Congress Must Not Shirk it's Responsibilities for Political Expediency

We realize that reaching agreement on an honest solution to the long-term challenges facing Social Security will be difficult, but the difficulty of the task must not prevent us from confronting it. Social Security reform will require us to tackle tough choices. We were elected to make tough choices, and our constituents deserve no less from us.

We hope that the suggestions contained in the legislation we have presented to you will help create a foundation to build a bipartisan agreement on Social Security reform. While our legislation may not be perfect, it does offer all of the elements that will be necessary for a responsible bipartisan deal to strengthen the Social Security system.

We do not agree with those who say that the issue of Social Security reform is dead. These hearings are evidence that the issue remains very much alive. More importantly, those of us who have the honor of serving in public office have an obligation to keep this issue alive for the sake of future generations that are counting on this system. As we tackle the tough choices that will be necessary to enact credible Social Security reforms, we must look beyond current polls and think about how our children and grandchildren will look back at the decisions we make today. We look forward to working with this Committee to create a future for the Social Security system that will make future generations grateful for the decisions we make today.

The Twenty-First Century Retirement Security Act: A Response to Issues and Concerns

Q. How is this bill different than last year's legislation?

A. We still adhere to the same guiding principles as before, a balanced, actuarially sound plan that reduces the $7.4 trillion unfunded liability in Social Security, and we create personal accounts that will advance-fund future obligations and implement much needed structural reforms. We've softened some of the painful elements of last year's bill and included some new provisions aimed at improving the retirement income of the working poor. Specifically, the plan:

- Eliminates the proposed mandatory coverage for state and local government employees.
- Eliminates the proposed reduction in spousal benefits.
- Eliminates the proposed increase in the normal retirement age to age 70. Under the Kolbe-Stenholm plan, the age at which an individual may begin receiving traditional benefits remains at 67 as with current law (although HR 1793 plan gets to age 67 faster than current law).
- Eliminates the proposed increase in the early eligibility age to age 65.
- Incorporates a version of the President's Universal Savings Accounts (USAs) by including a savings subsidy for low-income workers.

• Uses general revenues to help finance the transition to a partially-funded system. Uniquely, the Kolbe-Stenholm plan contains a self-financing revenue source. Ergo, the plan does not depend on uncertain, unproven budget surpluses.
• Implements more moderate changes in the bend points.

Q. What is the impact of the Kolbe-Stenholm reform proposal on the federal budget?

A. The 21st Century Retirement Act ensures that the Social Security program will operate on a solid, sustainable fiscal path well into the next millennium. It does this by honestly and responsibly addressing the unfunded liabilities of the program.

The legislation will result in a decrease in unified budget surplus totals in the near term since the plan uses a portion of current Social Security surpluses to advance fund future benefits through individual accounts. This short-term reduction in unified budget surpluses is more than offset by the long-term reductions in the unfunded liabilities under current law. The legislation will substantially reduce the budgetary pressures that begin in 2014 by reducing general fund liabilities by more than half, and placing the costs of the Social Security system on sustainable path. The plan would not affect the projected on-budget surpluses at all because it offsets the general revenue transfers to the Social Security trust fund with equal savings elsewhere in the non-Social Security budget, and does not double-count the Social Security surplus.

Three distinguishing characteristics separate this plan from other prominent proposals. First, unlike the President's proposal, the Kolbe-Stenholm plan restores the Social Security trust fund to 75-year actuarial balance. Second, unlike several "free lunch" proposals, the Kolbe-Stenholm plan addresses the cash deficits that begin in 2014, when benefit costs exceed payroll tax revenues. The plan reduces by more than 50% the existing $7.4 trillion general fund liability between 2014 and 2034, preserving the flexibility of future governments to meet other critical budget needs. Third, the 21st Century Retirement Act does not depend on projected budget surpluses, cost shifts or accounting gimmicks to balance the Social Security program.

Q. Isn't a "carve-out" further destabilizing to the Social Security program?

A. To the contrary, a carve-out enhances the long-term viability of Social Security *and* preserves other federal programs by preventing the enormous build-up of IOUs in the Social Security Trust Fund—IOUs that somehow must be translated into cash benefits. These IOUs are first claims on future federal revenue and can be funded only by increased taxes, reduced benefits, additional debt, or redirected spending from other programs (education, defense, environment, etc.). Under current law, the Social Security Administration estimates that at its peak, the Trust Fund will contain over $4.4 trillion in IOUs.

Rather than simply shift future Social Security liabilities to the operating budget in the form of Treasury bills held by the Trust Fund, the 21st Century Retirement Act draws down current surpluses to advance fund future benefits. Under the Kolbe-Stenholm plan, a portion of retirement income for future retirees will come from payroll taxes collected today and placed in individual accounts, instead of leaving the entire burden of funding retirement income to future taxpayers. In other words, our plan uses the current Social Security surplus to create individual accounts that will provide benefits for future retirees. These accounts are used to reduce the liabilities to the general budget beyond the actuarial deficit. This is done in lieu of investing the surplus in Treasury securities which merely creates a liability to the general government. By using the annual Trust Fund surplus to cover the transition costs of creating individual accounts, the plan is able to restore long-term solvency of the Social Security system and reduce the liabilities on future general revenues while preserving retirement security for future retirees.

Q. What is the impact of the Kolbe-Stenholm reform plan on national savings?

A. The 21st Century Retirement Security Act will increase private savings by encouraging individuals to save for their own retirement. In particular, the plan will enhance the ability of low-income workers to save by providing a federal match for voluntary contributions. In addition, the Kolbe-Stenholm plan strengthens public savings by using current surpluses to reduce future unfunded liabilities through the creation of personal retirement accounts, rather than spend the surplus on current consumption.

Q. What is the impact of the Kolbe-Stenholm plan on retirement benefits?

A. The 21st Century Retirement Act places the Social Security system on sound financial footing through a balanced, progressive package of adjustments to the defined benefit of Social Security, complemented by personal retirement accounts. The benefit adjustments are timed such that given a conservative rate of return, the bal-

ances that accrue in a personal account will at least compensate for the reductions in the defined benefit of Social Security. Vulnerable populations are insulated from the reductions in the defined benefit via a minimum benefit guarantee for low-income retirees and a savings subsidy for the working poor. Moreover, individuals who leave the work force to care for children, or for other reasons, may continue to contribute to their personal account, enhancing their retirement income. Current and near-retirees are unaffected by the changes proposed by the Kolbe-Stenholm bill. When all of the provisions of the 21st Century Retirement Act are taken into account, most future retirees will get a better deal under this plan than if we balanced the system solely by tax increases or benefit cuts.

Note: comparing the benefits afforded under Kolbe-Stenholm to the benefits promised under current law is extremely misleading. Current law makes promises that cannot be met without substantially raising payroll taxes. If Congress and the President do not act, current law benefits will be cut by 25–28% across-the-board in 2034.

Q. How does this plan benefit low-income retirees?

A. The Kolbe-Stenholm plan creates a protection from poverty within Social Security by establishing a minimum benefit provision. Anyone who has worked 40 years would receive a guaranteed defined benefit from Social Security equal to 100% of the poverty level, regardless of their earnings history. Retirees are eligible for the minimum benefit provisions if they have worked for at least 20 years. The minimum benefit provision guarantees a benefit of at least 60% of poverty for individuals who have worked for 20 years, and an additional 2% for each year worked, up to 40 years. If a retiree's regularly computed benefit is higher, they would receive the higher benefit. Individuals would be entitled to the minimum benefit regardless of the balance in their personal account. Moreover, the minimum benefit would be calculated without regard to any benefit changes, thereby shielding low-income workers from the reductions in the defined Social Security benefit.

The minimum benefit provision in the Kolbe-Stenholm bill will provide a stronger poverty protection than contained in current law. The provision is so strong as to effectively make the personal accounts a "bonus" for low-income people. Traditional benefits for the working poor under the Kolbe-Stenholm bill will be at least as strong as under the old system with no personal accounts, consequently, the personal accounts are merely an added bonus.

Q. How does the Kolbe-Stenholm plan benefit women?

A. The Kolbe-Stenholm bill contains several provisions that would be beneficial to women. Most notable is the minimum benefit provision (summarized above) that would provide a more robust benefit than what is afforded by current law. As a result of this provision alone, 50% of women and 10% of men will do better under the Kolbe-Stenholm plan than under current law.

This plan also allows for voluntary contributions. Workers are permitted to contribute an additional $2,000 per year to their personal account. Women who expect to take time off to raise children can make voluntary contributions both before and after their hiatus to "catch up." For women who earn less than $30,000, the Kolbe-Stenholm plan provides a savings subsidy. For the first $1 voluntary contribution, an eligible worker will receive a $150 match from the federal government. Each additional dollar is matched 50% up to a cap of $600 per year. For eligible workers who are unable to contribute voluntarily, the plan allows them to redirect a portion of their Earned Income Tax Credit (EITC) into their personal account to qualify for the savings match.

One of the reasons the Kolbe-Stenholm bill will be a better deal for women is the changing nature of divorce. Current law stipulates that if a marriage lasts 10 years or more, a woman is entitled to 50% of her ex-spouse's Social Security benefit. Unfortunately, not only has the divorce rate skyrocketed since 1935 when Social Security was first adopted, but marriages also are not lasting as long. Two or more decades ago, divorces were fewer and occurred after 15–20 years of marriage. Today, divorces are more likely to occur in the fourth or seventh year of marriage. Moreover, more and more women are not re-marrying. As such, many women are heading into retirement alone and without the benefit of a spouse's Social Security income. As more and more women are raising children alone and working in lower-paying jobs, the minimum benefit provision and the savings subsidy will do much to lift these women out of poverty.

Q. Does this legislation cut disability benefits?

A. No, the Kolbe-Stenholm plan leaves that issue to be decided elsewhere. The legislation sets up a mechanism under which Congress will have to vote before 2006

(when the bend point changes that affect disability would otherwise go into effect) on changes to bring the disability program into balance.

The bill provides for recommendations on disability to be made by the Trustees, in consultation with the National Council on Disability, to be acted on by Congress before our legislation affects disability in any way. Nothing in this bill affects the disabled unless the Council and Trustees agree that it should. Since none of our changes that could impact disability take effect until 2006, and we have required alternate recommendations before then, we leave plenty of time to deal with the disability issue.

Q. Why is it better to allow individuals to invest in the stock market? Why not, let the government invest the Social Security trust fund in the market?

A. Government investment does not address the national cry for personal ownership and control. Polls demonstrate very clearly that Americans want their own stake in the US economy and more control over their retirement benefits. The current system provides only a statutory right to benefits that Congress may adjust at any time. Only personal accounts offer workers ownership of constitutionally protected property.

Moreover, investing the Trust Fund in equities would cause risk to permeate the entire system. This is because the system's solvency—and the ability to provide basic Social Security benefits—will rise and fall depending on the performance of the stock market. If the market suffers a downturn in a year in which the trust fund ratio already is low, the ability of the Social Security system to provide benefits would be jeopardized. Under the 21st Century Retirement Act, the ability of the Social Security Trust

Once the federal government's balance sheet depends on the performance of the equities market, influencing the market up will become an unavoidable aspect of day-to-day economic decision-making in Washington. Political influences will be brought to bear on the choice of Social Security investments. There are significant consequences of the Social Security trust funds' acquiring significant ownership stakes in a large number of corporations. Moreover, government investment in private companies would conflict directly with the federal government's role as a regulator of industry.

Lastly, simply moving the Trust Fund into equities to duck tough choices would not add to national savings. If Social Security did get a higher rate of return, it would be at the cost of lower rates of return in the private savings system. In other words, it would just be a hidden tax on other investment, to fund current benefit promises of the federal government.

Q. How would the Individual Security Accounts be administered?

A. To reduce administrative cost and risks of fraud, the individual accounts in The 21st Century Retirement Security Act are modeled after the federal employee's Thrift Savings Plan. Investors would choose among broad-based funds including, for example: stock index funds based on the Wilshire 5000 or the S&P 500, a bond index fund, a blended index fund including both stocks and bonds, and a government securities fund. Accounts may be invested in any combination of the funds. Moreover, for those who cannot make an investment decision for themselves (due to incapacitation or other reason), there is a default option. The default portfolio would invest an individual's personal account 50% in the stock fund and 50% in the government securities fund.

Unlike government investment plans, this plan provides individuals with control over their retirement assets, including the freedom to invest is safe, risk-free Treasury securities. This plan does not force anyone to invest in the stock market.

Q. How will the funds that accumulate in an individual security account be distributed?

A. Individuals would have a variety of options for distribution of the funds in their personal account. Individuals would not be required to annuitize their ISA balance upon retirement unless they wanted to receive a lump-sum distribution from their account. To receive a lump-sum benefit, an individual must first annuitize a portion of their account such that when this annuitized benefit is added to their traditional defined benefit from Social Security, the total amount would provide a monthly income at least equal to the poverty level. Individuals are not required to withdraw non-annuitized balances upon retirement.

Individuals will be able to choose between a number of annuity plans that reflect the life needs of the individual. Concerns about shorter life expectancies among the poor can be addressed by requiring either a life annuity, period certain annuity or a refund annuity.

Q. Does the plan permit rollovers into individual retirement accounts (IRAs)?

A. Rollovers would not be permitted immediately. Once the system has matured to a point where administrative costs are predictable and manageable, rollover contributions from these personal accounts into individual retirement accounts would be allowed. The rollover accounts would have the same withdrawal rules as the ISAs, provided that these accounts are invested in broadly diversified low-administrative-cost funds.

Q: Does the plan allow early withdrawals?

A. No, the 21st Century Retirement Act prohibits pre-retirement withdrawals, other than for death or disability. The authors of the legislation are concerned that early withdrawal rules, such as pre-retirement or lump-sum distributions, would expose individual beneficiaries to increased risk of poverty, relative to protections that would have existed had ISAs not been established. Like Social Security, these benefits are strictly for retirement purposes. Other vehicles are available for individuals to access for non-retirement purposes. For example: workers may access IRAs for a first home, children's education or catastrophic health care costs.

Q. How does the CPI provision work?

A. The Consumer Price Index is used to index government revenue and spending programs for inflation, including Social Security benefits, Medicare premiums and elements of the tax code. The Kolbe-Stenholm plan assumes a temporary 0.33% reduction in the CPI below the estimates in the 1999 Trustees report. This adjustment is intended to correct for the bias in the CPI that most economists agree overstates inflation.

The legislation contains three basic provisions to achieve a more accurate CPI. First, it provides BLS with the resources and authority necessary to continue to improve the CPI. Second, it provides for the implementation of a time-lagged superlative index that will be used to compensate for upper level substitution bias that cannot be addressed in the existing CPI on a contemporaneous basis. Finally, the legislation contains Act contains a temporary legislated reduction in indexation of Social Security benefits that will be phased out as the bias in the CPI is corrected.

The correction in our plan is applied to all government programs indexed to the CPI. The net savings generated from reduced spending and accelerated revenue collections are then redirected to the Social Security program. In this way, the Kolbe-Stenholm bill avoids relying on uncertain projected budget surpluses, accounting gimmicks, and cost-shifting to infuse new revenue into the program.

The 21st Century Retirement Security Act

A Comprehensive, Bipartisan Plan to Save Social Security

Summary of Legislation

Create Individual Security Accounts

• Cut payroll taxes. Provides a payroll tax cut for all working individuals under the age of 55, by diverting 2% of payroll taxes into personal Individual Security Accounts.

• Enhance the progressivity of Individual Security Accounts by providing an additional tax credit for low-income workers. Workers who make voluntary contributions would receive a tax credit—to be deposited into their personal account—equal to $150 plus 50% of all voluntary contributions up to a cap of $600 per individual per year. This credit is phased out for wages between $22,500 and $30,000 a year.

Since the working poor largely are unable to save out of disposable income, this legislation would allow workers to divert a portion of their Earned Income Tax Credit (EITC) into an individual account and qualify for the additional tax credit.

• Allow voluntary contributions. Individuals would be permitted to save up to an additional $2,000 per year through voluntary contributions to individual accounts. As with the mandatory contributions above, there would be a tax credit equal to 50% of voluntary contributions of workers with taxable wages of less than $20,000 a year, to be deposited into their Individual Security Account.

Since the working poor largely are unable to save out of disposable income, this legislation would allow workers to divert a portion of their Earned Income Tax Credit (EITC) into an individual account and qualify for the additional tax credit.

• Use the Thrift Saving Plan model for administering individual accounts. To minimize employer burdens and administration costs, the individual accounts would be modeled on the federal government Thrift Savings Plan. Initially, investment options would include a stock index fund, a bond index fund and a Treasury securities index fund. Individual accounts could be invested in any combination of the three funds.

PHASE-IN REDUCTIONS OF UNFUNDED GOVERNMENT LIABILITIES

• Impose progressive changes in the current benefit formula. Slowly phase in bend point changes to reduce initial guaranteed benefit levels for middle and upper income workers. It is expected that these workers will generate balances in their individual accounts that will at least compensate for the reduction in guaranteed benefit. Because general revenues offset a portion of the transition costs, the changes in the bend points are more modest in the early years of the plan than they were in the 1998 legislation.

STRENGTHEN THE GOVERNMENT SAFETY NET

• Establish a new minimum benefit provision. Create a guaranteed minimum benefit for low-income workers more robust than current law. Social Security beneficiaries with at least 20 years of covered earnings would receive a benefit equal to 60% of the poverty level. This benefit would increase by 2% of poverty for each year of covered earnings, until the guaranteed minimum benefit reaches 100% of the poverty level for individuals who worked 40 years.

• The minimum benefit would be calculated without regard to any other benefit changes, thereby shielding low-income recipients from adverse effects of other measures taken to restore the Social Security system to solvency. Any income from the individual accounts would supplement this guaranteed benefit.

OTHER CHANGES TO REFLECT INCREASES IN LIFE EXPECTANCY

• Gradually increase in eligibility age for full benefits. Eliminate the hiatus in the scheduled increase the normal eligibility age, allowing the Normal Retirement Age (NRA) to reach age 67 by 2011. Both the Normal Retirement Age and Early Eligibility Age would be indexed thereafter to keep pace with longevity.

• Modify benefit formula to reflect increases in longevity. Create an additional actuarial adjustment based on increases in longevity. This adjustment would reflect the increased number of years individuals will live after reaching the Normal Retirement Age.

• Change the benefit formula to reflect the longer working lives. Gradually increase the number of computation years in determining benefit levels from 35 years to 40 years. For two-earner couples, however, this legislation would cap the benefit computation period for the lower wage earner at 35 years. This will benefit spouses who leave the workforce for child rearing or other purposes.

• Improve the actuarial adjustment. Currently, the delayed retirement credit does not compensate workers for the years of additional payroll taxes individuals pay while working past the Normal Retirement Age. This legislation would revise the actuarial adjustment for early/late retirement to reflect this.

REWARD WORK

• Eliminate the earnings test. Allow seniors who have reached the Normal Retirement Age to earn income without suffering a loss in their Social Security benefits.

• Count all years of earnings in calculating benefits. Include all years of earnings in the benefit formula in order to reward individuals for all income that they earn even if not among their highest 40 years of lifetime earnings.

OTHER PROVISIONS TO ACHIEVE AND PRESERVE SOLVENCY

• Provide for a more accurate Consumer Price Index. Provide the Bureau of Labor Statistics with the additional resources and authority necessary to continue to improve the Consumer Price Index. Use the superlative index that BLS will begin publishing in 2002 to adjust indexation based on CPI.

This legislation also would make a temporary change in the CPI to compensate for the remaining CPI bias until BLS is able to eliminate it. The legislated adjust-

ment in CPI would be phased out as BLS implements changes to eliminate the bias. The total reduction in CPI would be 0.33% below the 1999 trustees report.

The impact of this provision would be to reduce the rate of growth in cost-of-living adjustments and income tax-related parameters of the federal budget. This would create net savings in the non-Social Security budget and accelerate non-Social Security revenue collections. These funds will be used to offset part of the transition costs to a new, partially funded system.

- Recapture lost revenues. Credit all revenue from taxation of benefits to Social Security. The 1993 budget reconciliation bill diverted a portion of the tax revenue levied on Social Security income to the Hospital Insurance Trust Fund. Between 2010 and 2019, this legislation would slowly phase in the redirection of these taxes back to the Social Security Trust Fund where they belong.
- "Fail-safe" mechanism. Protect the program from once again falling out of balance by requiring Congress and the President to consider changes to the program on a timely basis whenever projections show deteriorating fiscal health for the trust fund.

Description of the Savings Subsidy for Low Income Workers

The 21st Century Retirement Act provides low-income workers an incentive to save beyond their mandatory contribution by providing a savings subsidy, or "match." A maximum of $600 per individual is allowed per year. To qualify for the subsidy in any given year, an individual must earn less than $30,000 per year and make at least $1 in voluntary contributions to their personal account. The amount of the subsidy is determined by (1) the amount of the individual's mandatory contribution, and (2) the amount of the worker's voluntary contributions.

Any worker earning less than $30,000 who makes a $1 voluntary contribution receives a savings match of $150. After that, all voluntary contributions are matched 50 cents on every dollar up to the maximum allowable match. In Example 1 below, the worker receives $150 for the first $1 of voluntary contributions. After the initial $1 infusion, additional voluntary contributions by the worker are matched 50% up to the maximum allowable match. The maximum match for the worker in Example 1 is $360 ($600 less the individual's mandatory contribution of $240). To receive the entire $360 match, however, the worker must voluntarily contribute at least $420. Contributions below this amount receive proportionately smaller matches (see the table below). All workers are permitted to contribute voluntarily up to $2,000 per year, however, the savings match for the worker in Example I would remain capped at $360 for any contribution over $420.

Example 1		Example 2	
Earnings:	$12,000	Earnings:	$18,000
Cap:	$600	Cap:	$600
Max Match:	=$600 -(2% x $12,000)	Max Match:	=$600 -(2% x $18,000)
	=$360		=$240
Mandatory Contribution: =$12,000 x 2%.	Mandatory Contribution: = $18,000 x 2%.	=$240	=$360

Voluntary Contribution	Federal Match	Total Contributions	Voluntary Contribution	Federal Match	Total Contributions
$1	$150	$391	$1	$150	$511
$100	$200	$540	$100	$200	$660
$200	$250	$690	$200	$240	$800
$300	$300	$840	$300	$240	$900
$400	$350	$990	$400	$240	$1,000
$500	$360	$1,100	$500	$240	$1,100

Total contributions = Mandatory Contribution + Voluntary Contribution + Federal Match. In Example 1, if the worker voluntarily contributes $200, Total Contributions = $240 + $200 + $250 = $690.

Since many low-income workers cannot afford to save out of their monthly paychecks, the Twenty-first Century Retirement Act allows workers to divert a portion of their Earned Income Tax Credit (EITC) to qualify for the savings match.

The savings subsidy of a worker who earns $18,000 is illustrated in Example 2.

Benefits of the savings match:

- Increases the retirement income of workers earning less than $30,000
- Encourages increased savings among income groups historically predisposed to dissaving
- Actually provides a mechanism for low income workers to save (the redirection of the EITC), rather than just providing an incentive to save
- Requires individuals to contribute to qualify—there is no "free lunch"
- Makes the personal retirement accounts more progressive

Strengthening Retirement Security for Low Income Workers

The 21st Century Retirement Security Act restores the solvency of the Social Security trust fund in a way that not only protects low-income workers from any reduction in benefits, it actually strengthens the safety net provided by the Social Security program. The Kolbe-Stenholm plan contains a new minimum benefit provision that offers stronger poverty protection than provided under current law. The plan also provides a subsidy to supplement the individual accounts of low-income workers. Finally, by addressing the unfunded liabilities of the Social Security without shifting new obligations onto general revenues, the Kolbe-Stenholm plan reduces the pressure to reduce funding for other government programs that benefit low-income populations.

- Strengthens the safety net through a new minimum benefit provision

The 21st Century Retirement Security Act contains a minimum benefit provision that provides a much stronger safety net for low and moderate-income workers when they retire than is contained in current law. An individual who has worked for 40 years and qualified for 40 years of coverage will be guaranteed a Social Security benefit equal to 100% of the poverty level. Moreover, any income from the individual accounts would supplement this guaranteed benefit. Widows would be covered by the minimum benefit guarantee based on his or her spouse's work history.

The new minimum benefit provision will enable Social Security to lift more of the elderly out of poverty than current law:

—50% of women and 10% of men would receive higher guaranteed Social Security benefits as a result of the minimum benefit provision in the Kolbe-Stenholm bill.

—Under Kolbe-Stenholm, no individual who works a full career will have to retire in poverty. Currently, nearly 8 million seniors receive benefits that are less than the poverty level.

The example on the following page illustrates the power and effectiveness of the improved government safety net. For a low-wage worker, the minimum benefit provision increases retirement income by more than 10%—not including any balances that would accrue in the worker's personal account.

- Expanded savings opportunity for low income workers

The individual accounts in the 21st Century Retirement Security Act will give low and moderate income workers the opportunity to benefit from investment opportunities that higher income workers already have with 401(k) plans, IRAs and mutual funds. To help low-income workers take advantage of this new savings vehicle the Kolbe-Stenholm plan provides a savings subsidy, or "match" for low-income workers who make voluntary contributions to their individual account. A maximum of $600 per individual is allowed per year. To qualify for the subsidy in any given year, an individual must earn less than $30,000 per year and make at least $1 in voluntary contributions to their personal account.

- Reducing pressure on other budget priorities.

The Kolbe-Stenholm plan will put the costs of the Social Security system on a more sustainable level that will protect other programs that benefit low-income families and prevent them from being squeezed out by the growing costs of the Social Security system. The plan makes the Social Security system financially sound without shifting costs to general revenues. Moreover, the 21st Century Retirement Security Act eliminates more then half of the liability to the general fund that will occur under current law when the system is projected to face annual cash shortfalls after 2014. By honestly addressing the budgetary pressures created by the unfunded liabilities of the Social Security system, the Kolbe-Stenholm plan ensures that future governments will have resources available to preserve funding for discretionary spending and other programs that benefit low-income families in addition to providing Social Security benefits.

Example: Impact of the Minimum Benefit Provision on a Low Wage Worker

Low wage worker earning 45% of the National Average Wage	$12,600 / yr
Current Law Social Security benefit	
Social Security Benefit at Normal Retirement Age: [1]	$568
Plus: Spousal Benefit (if applicable):	$284
Equals: Total Monthly Social Security Benefit:	$852
Social Security Benefit under Kolbe-Stenholm	
Poverty Level for a single-person household over age 65 [2]	$7,525
Translated into a monthly benefit (divide by 12)	$627
Plus: Spousal Benefit (if applicable)	$314
Equals: Total Monthly Social Security benefit	$941
Note: this amount does not include any balances that accrue in the workers personal account. Consequently, total benefits will be higher	
Kolbe-Stenholm increase over current law benefits:	$89 /month 10.4%

[1] Source: Social Security Administration, Office of the Actuaries Web Page http://www.ssa.gov/OACT/COLA/IllusLow.html

[2] Source: September 1997 data from the Bureau of the Census.

Why a Carve-Out is Necessary

Proponents and opponents of Social Security reform distinguish between the methods of financing a personal account with the terms "carve-out" and "add-on." The Kolbe-Stenholm proposal is an example of a carve-out: the personal accounts are funded by redirecting an existing portion of an individual's payroll taxes. An add-on uses new, additional taxes to f und the personal account. The diagram below illustrates the difference between a 2% carve-out and a 2% add-on account.

Because a carve-out would consume the Social Security surplus, it prevents the enormous build-up of IOUs in the Social Security Trust Fund—IOUs that somehow must be translated into cash benefits. An add-on, however, would allow the IOUs to accumulate. These IOUs are first claims on future federal revenue and can only be funded by increased taxes, reduced benefits, additional debt, or redirected spending from other programs (education, defense, environment, etc.).

In other words, a carve-out uses Social Security revenues to create personal accounts that will provide benefits for future retirees. These accounts can be used to reduce the liabilities to the general budget beyond the actuarial deficit, instead of investing the surplus in Treasury bills that create a liability to the general government. Most other plans focus on the actuarial deficit, which begins in 2034, without regard for the general budget liabilities that begin in 2014 (when Social Security begins to run a cash flow deficit). Under current law, the Social Security Administration estimates that at its peak, the Trust Fund—the general budget liability to Social Security—will contain over $4.4 trillion in IOUs.

An add-on consumes valuable federal dollars that otherwise could be used to implement structural reforms. Not only do the Trust Fund liabilities remain in place as described above, but an add-on uses general revenues that could be used to pay for the transition costs to a partially funded system. A carve-out, however, does not.

Moreover, by committing additional revenue to Social Security, an add-on only exacerbates the poor rate of return offered by the current system. By keeping the costs of Social Security within the current level, a carveout actually enhances an individual's rate of return.

Lastly, an add-on that is not used to offset future defined benefits (e.g. the President's Universal Savings Accounts) only aggravates Social Security's cash crunch by promising *more* than current low benefits. Without an explicit offset or advance funding of the system, future taxpayers will have to pick up the tab for both the add-on and the unfunded benefit promises.

A Fiscally Responsible Solution for Social Security

The 21st Century Retirement Act ensures the Social Security program will operate on a solid, sustainable fiscal path well into the next millennium. It does this by honestly and responsibly addressing the unfunded liabilities of the program. Three distinguishing characteristics separate this plan from other prominent proposals. First, unlike the President's proposal, the Kolbe-Stenholm plan restores the Social Security trust fund to 75-year actuarial balance. Second, unlike several "free lunch" proposals, the Kolbe-Stenholm plan addresses the cash deficits that begin in 2014, when benefit costs exceed payroll tax revenues. The plan reduces by more than 50% the existing $7.4 trillion general fund liability between 2014 and 2034, preserving the flexibility of future governments to meet other critical budget needs. Third, the 21st Century Retirement Act does not depend on projected budget surpluses, cost shifts or accounting gimmicks to balance the Social Security program.

• Restores the long-term financial security of the Social Security system

The 21st Century Retirement Act restores solvency of the Social Security Trust Fund by eliminating the entire projected cash shortfall in the trust fund over the next 75 years. Moreover, it does so using only the most conservative assumptions. Just as importantly, the 21st Century Retirement Act makes structural reforms to the Social Security system that help restore the traditional program to a path of long-term solvency that does not deteriorate over time. The Kolbe-Stenholm plan puts Social Security revenues and outlays on a sustainable course over the entire 75-year period. Lastly, the trust fund ratio—the amount of cash reserves in the trust fund relative to projected benefits—is rising at the end of the 75-year period. Thus, there is no "cliff effect."

• Protects the Treasury from the pressure of trust fund liabilities

Actuarial balance is only one measure of the financial stability of a Social Security reform plan. Just as important is the impact of a plan on the accumulation of IOUs in the Trust Fund, and the plan's reliance on these IOUs to pay benefits after 2014. Under current law, the U.S. Treasury must find $7.4 trillion in cash between 2014 and 2034 to finance Social Security benefits. These funds will allow Treasury to convert the IOUs in the Social Security Trust Fund into cash benefits for Social Security recipients. The 21st Century Retirement Act would reduce this liability by more than half. This feature is essential to the fiscal health of our government. Otherwise, future Congresses will be forced to cut other important government programs (e.g. education, defense, health care), or raise additional taxes to meet the obligations to our senior citizens. By contrast, plans proposed by President Clinton and others leave this liability in place and actually increase these general fund liabilities for the next fifty years.

• Does not rely on projected surpluses that may not materialize

Unlike other Social Security reform plans that are dependent upon funding from projected surpluses, the 21st Century Retirement Act is entirely self-financed and will achieve its goals whether or not current surplus projections are accurate. If surpluses do materialize, they would remain available for debt reduction, strengthening Medicare, tax cuts, or spending on other priorities. Plans which rely on projected surpluses either place the solvency of the Social Security trust fund in jeopardy or create problems in the non-Social Security budget if the surpluses are not as large as currently projected.

• Does not rely on accounting gimmicks

The 21st Century Retirement Act does not rely on double-counting, optimistic assumptions or other gimmicks to make the plan appear balanced on paper. Nor does the plan mask cost-shifts. All payroll taxes are used only once, either to fund current benefits, fund individual accounts, or credit the trust fund. Unlike other plans, the Kolbe-Stenholm plan does not use Social Security surpluses already credited to the Social Security trust fund to justify a second round of credits to the trust fund. Nor does the plan pay for individual accounts with funds that already have been credited to the trust fund, like some "free lunch" plans do.

This bill:

• Has been scored by the actuaries of the Social Security Administration as restoring 75-year solvency to the Social Security program

• Has bipartisan, bicameral support

- Preserves the existing benefit promises for current and near-retirees
- Increases the rate of return for all workers
- Enhances the government safety net
- Reduces Social Security's $7.4 trillion unfunded liability between 2014–2034 by more than 50 percent
- Does not rely on accounting gimmickry
- Does not rely on projected surpluses to create new general fund liabilities
- Establishes the opportunity for *all* Americans to create wealth
- Provides individuals with ownership of and control over their retirement assets—including the freedom to invest in safe, risk-free Treasury securities
- Rewards work

Chairman ARCHER. I have a couple of questions that I would like to inquire about. Do you guarantee the current Social Security benefits under the current law for all future beneficiaries?

Mr. KOLBE. We guarantee them for everybody. There is no change for anybody over the age of 55, and as is mentioned, the major change that we would make for those who are going to be the beneficiaries of the savings, the new personal accounts, would be the change in the bend points that affect benefits for those in the upper-income levels. Our view is that they get the benefit of the 2-percent accounts. They will see more benefit from that from the compounding effect of that.

There is actually, Charlie mentioned, an increase in the benefits for the low-income people. So we have actually made it somewhat——

Chairman ARCHER. No, I understood that, but I am asking a question that is applicable to all beneficiaries.

In the current law benefits under your program, are they retained for all future beneficiaries? I don't want it segmented, I just want an answer yes or no. Do you retain current law benefits for all future beneficiaries?

Mr. KOLBE. I think—if I understand what you are driving at—I think the answer is yes.

Chairman ARCHER. I don't see how you can, number one, but if you can, I would like to know how you do it based on the details that you have presented.

Mr. STENHOLM. Mr. Chairman, let me try you here and say the bend-point changes in our bill would reduce guaranteed benefits, if this is what you are asking, by 16 percent for average workers, 20 percent for high-wage workers, and 22 percent for maximum-wage earners. And the theory behind this is that those in that income category will benefit more from the 2 percent.

Chairman ARCHER. No, I understand the theory, I am just trying to understand the impact. So the average worker under your plan would receive 16 percent less in benefits than they would under current law.

Mr. KOLBE. In defined benefits.

Chairman ARCHER. Yes.

Mr. KOLBE. Correct.

Chairman ARCHER. In the Social Security benefits structure.

Mr. KOLBE. Correct.

Mr. STENHOLM. But, Mr. Chairman, the point is, we can't afford current law. So comparing it to current law——

Chairman ARCHER. I understand——

Mr. KOLBE. We get to 2035 before we have a reduction in benefits for everybody.

Chairman ARCHER. I understand we have got a problem in the program, that's why we are here today, and we are going to have to change the way we are handling the program. But the way you would change it would reduce benefits 16 percent for average workers.

All right, now, do you have the clawback that was talked about by the Senators to where the return on the carve-out would reduce the Social Security benefit?

Mr. KOLBE. With the return on the—no, we——

Chairman ARCHER. So your plan is different than theirs in that regard? I see your staffperson nodding. So I accept that as an——

Mr. KOLBE. It is different. That is one of the differences that I was going——

Chairman ARCHER. Well, I really had hoped that you all would highlight the differences in your testimony——

Mr. KOLBE. I could do that in just four quick—in less than 30 seconds.

Chairman ARCHER. OK. That's great. Go ahead.

Mr. KOLBE. The key differences between our bill and the Senate is that their benefit adjustments, the Senate benefit adjustments, are tied to contributions to the personal accounts. Ours are not. The minimum benefit is expressed through the creation of a fourth bend point.

We changed the bend points, they add a fourth bend point. They have KidSave, we don't have that. They will, we believe at a later introduction of their bill, will make an adjustment in the widow's benefit that we were talking about here so that the value for women would be the same as ours. But at the moment, as it has been introduced, it doesn't have that.

Their CPI change is greater. Theirs is half a percent, ours is 0.33 of a percent. And their—this is an answer I think to your question, Mr. Chairman, about creating another notch group. Theirs exempts current retirees, ours does not. So everybody, it would apply to everybody, the 0.33 adjustment.

Chairman ARCHER. All right, but you did not address the clawback. The Social Security benefit under your plan in contrast to theirs would not be reduced by the interest returned on the 2-percent carve-out.

Mr. KOLBE. That is correct.

Chairman ARCHER. So that is also another significant difference between your plans.

Mr. KOLBE. That is a significant difference. You are right.

Chairman ARCHER. All right, what are the dollar amounts of the benefit cuts in your plan over the 75-year period?

Mr. KOLBE. I don't think there is any way we can know that.

Chairman ARCHER. Yes, well that would be very helpful to us as we evaluate these plans and make comparisons. But it has got to be significant. The 0.33 percent CPI legislated adjustment is significant. In fact, it is major trillions of dollars over the 75-year period, and the 16-percent cut in benefits for the average worker has got to be significant.

Mr. STENHOLM. Mr. Chairman, your categories in that, that's the guaranteed benefit. And if you assume, which your question assumes a 100-percent loss of the 2-percent Thrift Savings Plan, then you are correct. That is a 16-percent loss. We don't assume that the Thrift Savings Plan is going to be——

Chairman ARCHER. No, I understand that.

Mr. STENHOLM. But your question is inferring that that is a 16-percent loss.

Chairman ARCHER. No. All that we can base our ultimate projections for Social Security on is the benefits structure for Social Security. And if the outside accounts produce more, that is wonderful, and that is a bonus. What is the impact of your program on the unified budget surplus over the 75 years?

Mr. KOLBE. There is, as we mentioned earlier, we do not take any of the funds from—we do not require any surplus funds in order to make ours work. There is no general revenue funds placed into it.

I'm not sure if that is entirely responsive to your question.

Chairman ARCHER. No, it isn't because whether we like or not, we do operate under a unified budget, and the impact on the unified surplus, which is the combination of the general Treasury and the Social Security fund is a very important barometer as we compare these various plans.

Mr. KOLBE. But I don't think there is—is there any CBO estimate for surpluses over 75 years anyhow? How would you do that over 75 years?

Chairman ARCHER. Well, all I can tell you is that the Archer-Shaw plan has a unified budget surplus increase of $122 trillion over 75 years. And I just want to compare the various plans as to their impact on the unified budget surplus. You may not have that yet because SSA has been under a lot of pressure to get all of these projections and estimates out. And that may be forthcoming in the future.

If you don't have it, I understand that.

Mr. KOLBE. One of the things, Mr. Chairman, that I think it is important to keep in mind is that the CPI adjustment of which there have been several questions about here today, is a critical component of ours. It is really a self-generating revenue source.

Chairman ARCHER. No, I understand that. But it also is a tax increase on middle- and low-income workers, which is another undesirable aspect.

Mr. KOLBE. Except that we would tie everything to the CPI, including your Medicare premiums would not be adjusted as much.

Chairman ARCHER. I understand, but there would be additional revenue taken out of the taxpayers of this country, particularly more heavily on middle-income tax payers as a result of not getting the CPI as provided under current law.

That would be a tax increase on middle-income workers in this country and would further fuel, of course, the moneys coming into the General Treasury. That's an unfortunate byproduct of changing the CPI.

Mr. Shaw.

Mr. SHAW. Just very, very briefly, Mr. Chairman, just to explore further what you are talking about. When you look at this as 1

year, it doesn't really amount to a whole lot, but when you take this over a 10-, 20-year period, you are really talking about some real money as far as the bracket creep.

And as far as one of the things I am really concerned about is the creation of a new notch, where future retirees—yours is not in there as in the Senate bill?

Mr. KOLBE. Yes, we would not create that notch in ours.

Mr. SHAW. All right, then I congratulate you for that because that has created major heartburns for all of us. Before I was Chairman of the Social Security Subcommittee, I used to forward those letters to the Chairman. Now I have no one to forward them to.

But that was a terrible political mistake that was made back in the seventies, and I am glad to know that our Chairman voted against it at the time.

Thank you, Mr. Chairman, I yield back.

Chairman ARCHER. Mr. Matsui.

Mr. MATSUI. Thank you, Chairman, I want to try to understand this. I want to commend both of you, I know how difficult it is to come up with a plan like you came up with, and obviously the four Senators before you, because you make the tough decisions. And I think some of the dialog that we have heard with respect to your plan would be the kind we would hear in the 2000 campaign if, in fact, Members got involved with adjustments in benefit levels.

But what I see in your plan is an attempt to integrate your proposal and try to deal with this issue in the overall Federal budget over the next 75 years, and what is troubling to me about Mr. Gramm's plan and the plan that Chairman Archer and Mr. Shaw have, which I believe is credible—both are credible—is the fact there are significant risks to the economy and, obviously, to the Federal budget if those plans are implemented because they take significant sums of money in the first 30, 40, 50 years. Payback occurs in the last 20 years, but the first 50 years it is trillions of dollars that go from the general fund, if there is a general fund surplus, into the Social Security fund.

And if we do not witness a surplus, if we have a deep recession, much deeper than anyone projects, it could be catastrophic to the budget but particularly to the economy. Your proposal, I believe, somewhat ensures that if you do have a deep recession, that would not necessarily happen, and I would like you to discuss a little bit about programs that don't have any cuts in benefits and don't have any payroll tax increases and how we make up the 2 percent payroll problem over the next 75 years. I mean, help me with this, because I understand what you are trying to do. Maybe, politically, it is very difficult to do what you are trying to do right now, but there is a lot of merit in what you are talking about, and you are the first two, and, obviously, the four Senators were the first four to come up with a plan that at least tried to deal with the next 75 years, not just in terms of the Social Security problem but also in terms of the overall budget, and certainly the overall U.S. and perhaps international economy.

Mr. STENHOLM. I will refer you back to our chart to show the difference between current law and our bill and what it frees up; the unified budget, the question the Chairman was talking about. These are real dollars that have real effects on the surplus. Also,

our plan, as you correctly have stated, we do not rely on the economy and projections of the economy. We have had a little bit of concern—you remember it hadn't been too long ago that we were basing our projections for budget purposes on 1 and 2 years, and then we went to 5, and then we discovered that we got real good at backloading. In other words, you would take a proposal and it would spend low or if it was tax cut, it would have less effect for the 5-year, but then the sixth, seventh, and eighth, it would literally explode. And we said, "Let us learn by that, and let us make sure." as I said in my statement, the 75-year solvency is important, but it is not the most important. What do you have at the end of the 75 years is critical.

And, therefore, in our proposal, we do make some tough choices, and it is easy to criticize, and it is rather amazing to me having spent a good part of the time with many of my folks here saying that unless we really—you know, if you get a dollar this year and you get a dollar and a dime next year, you have got an increase. Now, all of a sudden we are arguing that unless you get a dollar and a dime we are cutting. That is difficult for me to understand, and I think the American people to understand that, and, therefore, what we are saying is let us take a 75-year honest projection; let us make some adjustments; let us hold harmless anyone 55 years of age and older from any significant changes in this, significant, but let us recognize that what we have to do is solve the problem for the 20-year-olds simultaneously and do it—and, again, I refer, Bob, to this chart right here. It shows what CBO has scored what we do as far as the specific question of fiscal responsibility that you asked, and a picture is worth a thousand words.

Mr. MATSUI. Jim.

Mr. KOLBE. I would just concur that I think the key that is a key difference, there are differences between ours and Chairman Archer and Mr. Shaw's proposals, and that is certainly a key one that we don't rely on presumptions about what the economy does. If you have zero return on your personal accounts, you would still have a solvent plan under what we have proposed, but, again, I want to say that I think all of these proposals have merit in that they are at least going in the direction I think we need to be looking at.

Mr. MATSUI. I thank both of you.

Chairman ARCHER. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman, and let me begin by commending my two friends, Mr. Kolbe and Mr. Stenholm, for going about it the right way by working together in a bipartisan way. As we look at Social Security, I think we all agree that when it comes to bipartisanship, this is one of the areas we should begin with bipartisanship and finish up with bipartisanship. So, I commend you, and, of course, I also acknowledge from my experience with town meetings, particularly with senior citizens, you chose the more painful path in putting together your plan and your solution that you are offering today.

You know, one of the attractions of the concept of the personal accounts that I hear as I travel throughout the south side of Chicago and the south suburbs is the thought that if you have personal account as part of your Social Security portfolio, that if for some reason you don't live long enough to collect it, that it becomes

part of your estate and is passed on. How do you treat your accounts? Do they become part of someone's estate that they are passed on or is it lost?

Mr. KOLBE. No, it is not lost. It is included in your estate. When you retire, you can take your pay out from your account in at least two different ways. One, you could annuitize it. You could annuitize only the amount necessary to guarantee you a poverty level payment, and the rest you could take as a lump sum if you want to travel around the world. You could buy an annuity, which, of course, would guarantee benefits over a set number of years, in which case if you died the next year——

Mr. WELLER. So, you are saying you could buy a second annuity with the amounts above the——

Mr. KOLBE. You can take—there are two basic ways. You can either annuitize all or part of it or you could take it as payouts from cash payouts from the Social Security Fund over the life expectancy, in which case, the amount in your account goes to your heirs. If you annuitize it, it depends on what kind of annuity you buy. Say you bought an annuity that guarantees payments for 20 years; you died the first year; those payments continue to your heirs for the next 19 years over that. So, it just depends—and you could annuitize an amount only necessary to get the minimum benefit, the poverty benefit, and you could take the rest of the cash lump sum. You could take all the rest. Let us say you had $400,000 in there with earnings in your personal savings account. You could take an amount necessary that would—let us say it is $200,000 necessary to buy an annuity that would guarantee a minimum poverty level benefit. Then you could take the other $200,000 as cash; start a new business; go off around the world; buy a houseboat; do whatever you wanted.

Mr. WELLER. How would it be distributed? If you passed on, how would it be distributed to your heirs? Is there an automatic assignment? Automatically, it would go to your spouse or, automatically, it would go to the children? Do you have to designate, make a choice yourself, at sometime in your life?

Mr. KOLBE. In our legislation, this has not been so specific as to define the exact mechanism by which you go about doing that, but it would be as it would be in any current law with anything that is in your estate. I mean, you would be able to assign it in the same way.

Mr. WELLER. OK.

Mr. STENHOLM. I would assume it would become part of most wills in the direction of that. That would be my assumption, but we have not dealt with that specific as this.

Mr. WELLER. I know you use the Thrift Savings Plan as one of the models you have been looking at. Of course, there is probably a formula for that, I believe for the treatment of that as part of someone's estate.

You also make some changes in some areas regarding the retirement age, and can you just review again how you adjust the retirement age as your proposal? I was born in 1957. I believe the change that is currently in place for retirement age for those born after 1960, I believe, are the ones who it is adjusted currently to

when they become eligible at 67. I was just wondering if you can kind of walk us through that?

Mr. STENHOLM. We don't change current law, the 67. Last year's bill, we proposed going to 70, and paid dearly for that from folks that disagreed with that. So, this year, we said, "No, let us keep it at 67," but we increased our shortened period of time. I believe today it is 2021. We speed it up to reach the retirement age at 2011, 2 months per year beginning in 2000 or whenever the bill should become law; 2 months per year. So, if you were 65 in 2001, you would have to be 65 years and 2 months. Or if you are 64, you can do your own computation as to that.

But, now, you can retire at any time you wish. One of the misnomers that gets in that we are saying when you can retire. You can retire at age 52. It is when you are eligible to draw your guaranteed benefit that is affected by that, as everyone here knows, but a lot of the general public tend to listen to the rhetoric that says we are changing the retirement age.

Mr. WELLER. Just a quick follow up on that. To access the personal account, do you have to be 67 or can you——

Mr. KOLBE. No.

Mr. WELLER. You can access that when you are 50 if you choose to retire.

Mr. KOLBE. Fifty-one if you want, as long as you have enough in that personal account that there is an annuity equal to the poverty level benefit.

Mr. WELLER. Thank you.

Chairman ARCHER. Does any other Member wish to inquire?

Mr. RANGEL. Yes.

Chairman ARCHER. Oh, Mr. Rangel.

Mr. RANGEL. I want to thank both of you for the leadership that you have demonstrated over here and especially now in a bipartisan way in getting real attention to your program.

You said Charlie Stenholm, that with any plan, wherever there is any controversy or reduction in benefits or cost, it appears as though hearings like this would highlight that. The unique thing about your presentation is that as both of you know, if we were to pick this thing apart, there would be enough controversy to talk about, and that is going to be true of any package that is put together, whether we were talking about Mr. Shaw's package or the President's package or your package.

The only way to get this done this year is for us to have to admit that whatever pain there is in there, it is for the good of the solvency of the program in the long run. As I told Senator Moynihan that even with some of the things that he was talking about with the CPI, if he had an opportunity to talk about a package rather than an item, it doesn't take that much political courage to pick the program up off the ground. But it just seems to me that if each person was to talk about their own package without us coming together to talk about which things we can work with and which things we can't, we are not going to get out of this this year, and we certainly won't even think about touching it with a 10-foot pole next year.

Senator Moynihan had suggested that when this issue came up before—I think he said 1983—that Senator Dole just picked a cer-

tain number of people from the Finance Committee, put them together, and in 12 days they came up with something to resolve what was a crisis, and he further suggested to us that we not wait until there is a crisis.

My question is: We can continue to have these hearings, but could you give any suggestions or recommendations to this Committee as to how we can come forward in a bipartisan way, which certainly would include the President's people, to come up with a package that we can take to the floor? The reason I ask is that there is not a witness that can come before us who will not be asked about some type of problems with his package if that is what we are looking for.

Jim.

Mr. KOLBE. That is wonderful question; it is hard. It is the most difficult question of all, Mr. Rangel, and I wish I had an easy answer for you. I think, however, what has to happen is two things. One, I think the pressure to do something is going to grow and for the reasons that I mentioned at the outset of my remarks—I am not sure that you were here—and that is, in a few weeks, I think it is going to begin to dawn on people in this body that the only key to solving the budget problems and the hope to give tax relief to American citizens is to solve Social Security reform. The lockbox we passed last week, no matter whether you were for it or against it, is illustrative of that, because it says once you solve—have a Social Security reform, you can open the lockbox and you can do with the surplus what you choose at that point if you have a reform that works. So, I think that is absolutely the key, and I think that is going to drive Members of this body toward a solution.

I think that what has to happen is people from this Committee, this Ways and Means Committee, have to, as you just suggested, engage with the President's people quietly to try to find some ground on which they can do serious reform, and I think those discussions have to start, and they have to start now, and I believe the President has to stand up to the plate and take a position of leadership on this and publicly on this issue.

Mr. STENHOLM. You have asked the tough question and one of which, while we haven't gotten to that point as yet, Mr. Rangel, but if there is some way that we can put together the skeleton of a proposal that deals with the fiscal responsibility of the solvency as well as the long-term concerns of all of us who have concerns about Social Security, then it must take Presidential leadership, which, I have to say, I was rather disappointed that we have not received that kind of leadership as yet from the White House, and I say that publicly and privately. I understand why, for the same reason that anybody proposes anything—you get shot at. I went through that in the campaign last November. I was shot at severely because of the support for this program, but you will hear from Mark Sanford and Nick Smith and Jim Kolbe, and I had friends on the other side of the aisle that came to my defense against colleagues on the other side of the aisle that attacked me for this of which I will be eternally grateful, and it is that kind of spirit, Charlie, that I think has to go into this question.

We have to be willing to bend a little; be willing to compromise in some very strongly held positions; find the leadership simulta-

neously with the leadership of this Committee and the administration, and then find some followership, and Jim and I are here on behalf of our bill. It is bipartisan, it is bicameral, and we are willing to be followers. We don't pretend we have got all of the answers, but we do think we have given you a framework under which you can work. But that is up to you and this Committee to decide how that will be done. All I guess I would say to you is we are willing to help in any way in which you believe will be constructive.

Mr. RANGEL. Well, we have got one tall partisan wall to jump over if we are going to come up with a bill. The President didn't ask any Republicans for their ideas about Social Security, and the Republicans on this Committee certainly didn't ask any Democrats for their ideas. So here we are listening to everybody's proposal, which is educational, but if we are going to come up with a bill we have to decide that we are going to break some eggs and move forward together with everyone there—the White House, Republicans, and Democrats—so that we don't have any losers, because at least we were trying. No matter what is in each bill, we don't have to adopt anything until we adopt it all. Please don't give up on us, and keep encouraging us and, why, me and the Chairman, why, we talk almost every day now, so that is movement.

Mr. KOLBE. And if I might just say, that is what I think what commends our proposal is that it is the only one that is House and Senate and has Republicans and Democrats on board, so we have been talking to each other.

Chairman ARCHER. The gentleman's time has expired.

Mr. Hulshof.

Mr. HULSHOF. Thank you, Mr. Chairman. Mr. Stenholm, I am going to accept your invitation not to nit-pick certain elements here, but I do want just some general clarification on a couple of things, and I have got the piece that your staff has put together and specifically some of the changes in your legislation this year as opposed to last year, and I want to applaud, by the way, as I understand, under your first bullet point, that this year's version of the Kolbe-Stenholm bill eliminates the proposed coverage for State and local government employees.

Mr. KOLBE. Correct.

Mr. HULSHOF. And, certainly, Mr. Stenholm, you are aware that in your home State, we have heard on the Social Security Subcommittee from representatives of a retirement system that has opted out in Texas that has been very successful. What went into the thinking to make this change? I mean, I applaud the change, but I mean——

Mr. STENHOLM. Well, in my case, I had about all the hide I could give up from the country on this one——[Laughter]

And decided that——

Mr. KOLBE. It was clear that several delegations from several major States were going to have a real heartburn with this provision. We had to find a way to make a change in it, and we did.

Mr. STENHOLM. You know, I would say, I continue to engage in dialog with my Texas concerns with this, and I will forever believe that there is a way in which it can be done and done to the benefit

of the Texas employees, and so forth, but I have not been successful in convincing them; therefore, we changed our mind.

Mr. HULSHOF. Let me ask this clarification regarding the disability benefits. I am hopeful and I am confident that probably in the near future that the Social Security Subcommittee and hopefully this Full Committee will be considering some changes in our Federal structure to remove disincentives for those with disabilities that return to the work force. Obviously, the Senate has been moving. I think in *Congress Daily* today it talks about the progress on that side, and there are several Members on this Committee on the Ticket to Work provisions and trying to really help those individuals with disabilities rejoin the work force. It is my understanding, in your legislation, that disabled workers are exempted from some of the provisions but not all, and I was hoping to get some clarification as to are we talking about a cut in disability benefits or what are we talking about as far as the disability community is concerned?

Mr. KOLBE. The answer to that is both yes and no. We have no immediate cuts to disability. We will freely concede, we do not address the disability issue here. It obviously has to be addressed. The legislation sets up a mechanism that Congress would have to vote before 2006, which is the year that the change in the bend point would begin to affect disability payments, so that by the year 2006, we would have to do something to bring the disability program into balance. It also further provides for recommendations to be made by the trustees of the Social Security Trust Fund in consultation with the National Council on Disability to be acted on by Congress to do that. But we do not solve the disability problem here.

Mr. HULSHOF. OK. Mr. Stenholm, anything else you wanted to add to Mr. Kolbe's answer?

Mr. STENHOLM. No, the National Council on Disability is the proper vehicle to give the advice and counsel in making those changes and for proposals to the Congress for specific action in answering your question.

Mr. HULSHOF. OK. Thank you, gentlemen. Thank you, Mr. Chairman. I yield back.

Chairman ARCHER. Mr. English.

Mr. ENGLISH. Thank you, Mr. Chairman. Briefly, I want to join everyone else in thanking the gentlemen for testifying, having putting so much effort into putting together a balanced plan.

One of the objections that we hear raised to individual accounts, such as the ones in your plan, is that they will increase administrative costs relative to the current system. I would like you to comment on that generally and also comment on the advantage relative to other plans of the very narrow menu of investment options that you allow. You essentially allow three different accounts and permit people to portion their resources between those three investment systems. Can you comment on the administrative cost question and also what is the appropriate number of investment funds to make a system like this work and be competitive?

Mr. KOLBE. I will take the first part; maybe Charlie would like to answer the second. The cost of the Thrift Savings Plan, which we have modeled it after, is one-tenth of 1 percent in the adminis-

trative cost. It is extraordinarily low, because it does invest in index funds, not in picking and choosing particular stocks. You don't have that kind of management cost. It is like Social Security; it is strictly the administrative cost of the accounts.

As far as the numbers, Charlie, do you know? Go ahead.

Mr. STENHOLM. Well, you know, first a little background. When I first entered into this, I was rather opposed to individual accounts and privatization. Jim was much more ardently supportive of this, but we listened to a lot of experts, and we had a lot of help. The Center for International Studies and a private commission of some of the experts in this business have given us the advice and counsel to put together both the Senate plan and our plan that we have ultimately cosponsored. In doing that, it ultimately came around to the Thrift Savings Plan as a pretty darn good example. If it is good enough for Federal employees and Members of Congress, what is wrong with having that available for every citizen of the United States? You look at the cost of that—the administrative cost of our Thrift Savings Plan is very, very low. It is true it has narrow opportunities for investment today, perhaps, by some standards, but keep in mind, it is intended that will grow over the years, too, as the Thrift Savings Plan continues to grow and to flourish. So, that is kind of the background. I have forgotten your specific question on the——

Mr. ENGLISH. Do you generally feel that administrative cost is a serious argument against individual accounts?

Mr. STENHOLM. It is a very serious argument against some proposals for individual accounts particularly for those small accounts, because you can literally have administrative costs being a substantial part of individual small accounts. But, on the whole, if we stay—in our opinion—if we stay close to the concept of the Thrift Savings Plan, it is irrelevant and will become more so, and those who oppose individual accounts will gradually come around to believing that it is not the problem that the more ardent opponents today would say.

Mr. KOLBE. Mr. English, as far as my response on the different investment opportunities you might have, my answer might be a slightly more political answer, and that is I would certainly have no objection to a broader range, but I think we have a real problem. We have to acknowledge we have a real problem in this body of getting some of our colleagues over the hurdle into the idea of any kind of personal retirement accounts or individual accounts, and limiting it to the kinds of options or modeled after the Thrift Savings Plan, I think is something that will give a lot more people more comfort level.

Mr. ENGLISH. One last question, and I would invite you to give me a brief answer on this. One of the very difficult issues you tackle in your plan is to provide for the adjustment of the normal retirement age, and this is particularly explosive in a community like mine where you have people who work on the shop floor, who work in very strenuous jobs, and who are ready to retire at 62, if not earlier. They are physically no longer able to exert themselves the way they previously did. I wonder, as Americans live much longer and we think that people's ages are going to increase considerably as medical science improves, is it realistic to continue to adjust to the

normal retirement age if we continue to have a substantial manufacturing economy? And I invite you to answer very quickly.

Mr. STENHOLM. You know, last year, we proposed the 70-year normal retirement. This year, we are saying the 67, and we are not changing the 62. Last year, we proposed changing the 62 to 65 for the reasons you mentioned. But here is a thought for us to continue to think about in regard to the people that you represent and others: clearly, there are occupations that do not lend themselves to continued productive work to 67 and 70. We are told by people who keep these statistics that that is somewhere between 10 and 25 percent of the work force. It seems to me we would be better off dealing with the disability side of this question and allowing for provisions for those individuals, and I represent many of them also, that it would be taking a rifle shot to those individuals and providing for their unique needs rather than continuing to suggest that everyone must continue to wait until early retirement or 62 or 67. That is the concept.

Mr. ENGLISH. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Portman.

Mr. PORTMAN. Thank you, Mr. Chairman. I will be brief.

I want to start by commending the authors and the others you have managed to find on both sides of the aisle to help you on the Social Security front, particularly what you have done with individual retirement accounts. The Congress, I hope, will be catching up with you. I think the American people are starting to catch up to you, but you were out there early on.

I have a number of questions, but I maybe will talk to, Charlie, you and Jim on the floor about the specifics, but let me make one comment and then ask for your input on it. With regard to the individual accounts, the ultimate goal of all of this is retirement security and to help people to have the kind of resources they need to have less anxiety and more comfort and security in their retirement. Our private system is in trouble today, as well; that is the employer-based system which is the third leg of the stool, and actually more benefits were paid out under that last year than Social Security. Only half of American workers now have any kind of pension.

One of my concerns with USA from the start, the way the President proposed it, was why should an employer, particularly a smaller employer who is already under some crunch trying to administer all the rules and complexities and problems of the 401(k) or even some of the more complex systems of the defined benefit plan, for instance, want to continue to even offer this if the government is going to step in and do it?

Now, under yours, you have the ability for people to add $2,000 a year to their individual account, but you also allow the government to match, and you start with a pretty healthy match for low-income workers and then it goes to dollar for dollar match. Under the private system—and this is really my comment; just for you to look at this—because of the way the nondiscrimination rules work, unless you get workers who have incomes at the lower and middle end into your retirement plan, you cannot have a qualified retirement plan, and those rules are put in place for good reason. You

don't want just the high-end management folks to take advantage of the tax deduction and not spread it out through the work force.

So, my concern is, number one, you are going to have some employers who are going to say, "Gee, the government is going to take care of it; I am not going to worry about it." Second, you are going to have some plans that are going to be disqualified, because they won't be able to meet their discrimination testing, because the lower paid workers are going to say, "Why should I participate in this plan even if there is a decent match from the employer," and in some cases there isn't, "when the government is now taking care of me?" And I would just ask you to look at that. On the USA side, the administration is trying to address this by giving companies some kind of a credit. I haven't seen the specific language, but they understand that is a problem. I am not sure they have addressed it, but I would just ask you to, as we go forward, take a look at that and solicit any comments you have today.

Mr. KOLBE. Yes, I think it is something for the Committee—it is a good question. I think it is something very much worthwhile looking at. I don't believe we are creating a disincentive in here for private pensions. There is no tax advantage in our accounts, and so I don't think we have created a disincentive for it, but I need to think about that question a little bit more.

Mr. PORTMAN. I think there is a way to do both, and, obviously, the way I feel about it is we ought to also compliment this proposal with changes in the private side to make it work better, because if you reduce some of the regulations and increase limits and make it more attractive, you can do both. But under our current system, I am afraid it would be displacing private income, and the reason that is a problem, in part, is because a lot of that is leveraging private dollars now. In other words, it is not the taxpayers paying it; it is matches and people's decision to set money aside that the government doesn't even subsidize. Some of it is subsidized through a deduction. It is just a thought as you go forward.

Mr. STENHOLM. It is a valid thought. Just on comment on that, something that we have discussed many, many times. How many of us at sometime in a speech have said that Social Security was never meant to be a retirement program; it was meant to be a social insurance program and to provide supplemental. I envision what we have the opportunity of doing this year is revisiting that and doing it in a way that we take the other, the private side—the other two legs of the three-legged stool, as we often refer to it—and encompass those in one in which it does not become an disincentive. The commission that worked with us on this talked about this and came to the conclusion that that is something that is best left out of the bill at this stage. So, therefore, I concur, I don't believe that we do create a disincentive in this for anyone, but your thought is very valid.

Mr. PORTMAN. Thank you. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Watkins.

Mr. WATKINS. Thank you, Mr. Chairman. Let me begin like all the other family Members here on the Committee have said thanks for your efforts and what you are doing, and I salute you for all the hard work; it is a tremendous amount.

I have just two quick questions, and you probably have already felt these through; if not, let me simply—what is the—on withdrawals later on, what it the method of taxation? As ordinary income or as capital gains?

Mr. STENHOLM. It is intended to be the same as nondeductible hours.

Mr. WATKINS. As nondeductible hours.

Mr. KOLBE. Meaning you are taxed on your buildup but not on your contribution.

Mr. WATKINS. Yes. Just dealing with it as kind of a Roth-IRA or not, and it could make a difference on scoring some stuff later on as you are going through it. I just kind of wondered how that might be addressed in your plan.

Mr. STENHOLM. Ours has been scored from the standpoint of a nondeductible hour.

Mr. WATKINS. I know there are some variable annuities that are as ordinary income, and a lot of the IRAs are as capital gains, of course.

And, then, the other one was what method did you use in figuring the poverty level—adjusting for the poverty? Is it——

Mr. KOLBE. That is Census Department data for the poverty level. We use the Census Department.

Mr. WATKINS. That could make a big difference also when, as we know right now, a lot of Social Security are in poverty.

Mr. STENHOLM. Eight million of today's beneficiaries on Social Security receive Social Security guaranteed benefits that put them below the poverty level. Under the bill we proposed, no one that has worked their lifetime will find themselves with a guaranteed benefit less than the poverty level.

Mr. KOLBE. The determination—as I understand it—the determination of that poverty level, whether it is for senior citizens or whatever, is made—incomes for a family of four, a family of three or whatever is made by the Census Department, their data, collection of data.

Mr. WATKINS. That could be a big variable in a lot of the programs and all along the way right there.

I admire a lot of the senior citizens who are literally getting by on $350, $400 a month. They stretch that dollar more than any human being I have ever seen, including my mother who is on that, and I remember a tough vote here one time where we were criticized a great deal, and people called her and talked to her about her son being in Congress and the decision he is making and said that I should get out of Congress if I couldn't do certain things. So, I called her the night before one of the big votes, and I told her, I said, "Mamma, they are giving me a lot of criticism; probably have marked that I am not going to vote." I went through a lot of the economic jargon of economic assumptions and the variables of the budget and all the things that went into it, and my mom is a lady who had very little formal education, but she is a woman with a world of wisdom and getting by just on minimum Social Security, basically. And she said to me, she said, "I don't understand a thing you are talking about. You take care of the poor, the blind, the disabled, and you do what I have told you, and the rest of us will get along OK." And she never looked at herself as having any kind of

problems. So, I just kind of wondered how that adjustment is going to be made there on poverty, because it will make a big difference in the lives of a lot of people.

So, thank you very much for what you have done.

Mr. STENHOLM. You have put your finger on one of the predominant forces in our bill of trying to recognize that those in the lower income and the poverty level and retirement—that, to me, is one of the strengths of the bill that we propose to you today.

Mr. WATKINS. It should be looked at very seriously. Thank you.

Chairman ARCHER. If I may briefly just follow up on that last line of inquiry, because I think all of us are sensitive to trying to be sure that people who are senior citizens are getting adequately taken care of, particularly in the low-income levels, but the Concord Coalition has reiterated many, many times that they thought that we ought to have a means test on Social Security, and I personally disagree with that, but the current law provides that the Federal Government has a poverty program for those who pass a means test to get to the poverty level through the SSI Program, so that the Social Security benefit does not equal the poverty level. All they have to do is show need, and they get an SSI Program that gets them up to the poverty level.

Now, under your plan, you would be entitled to the poverty level as a matter of entitlement irrespective of your means. So, an individual who had a large amount of income or a large amount of assets would still get a higher benefit than they would get under the current law as a matter of entitlement, as I understand it. Is that incorrect?

Mr. STENHOLM. That is incorrect, Mr. Chairman. Again, you make an inference. Only that individual that works 40 years is entitled to a Social Security guaranteed benefit equal to the poverty level.

Chairman ARCHER. All right. OK, but that still would qualify people who may have received some sort of largesse in the way——

Mr. KOLBE. Like when you win the lottery?

Chairman ARCHER. A lottery or someone who had received as a beneficiary of a will, financial need would not be involved in that. It would be automatic, and it would be a matter of entitlement under the law irrespective of the financial worth of that individual. The current law today takes care of the people you are talking about through the SSI Program.

Mr. STENHOLM. I believe only up to 75 percent of poverty, though, if you will—I believe I am correct, and you certainly know more about this than I do, Mr. Chairman——

Chairman ARCHER. Well, anyhow, that is just a matter of some thought that you might work through as you continue to work on your program.

I do thank both of you. I think you have done a tremendous amount of work, and you are making a very, very constructive contribution to this entire consideration, and I appreciate your testimony today.

Mr. KOLBE. Thank you for your attention and for the good questions, Mr. Chairman. It was a good hearing. Thank you.

Chairman ARCHER. Mr. Nadler. Oh, it is—I am sorry, Mr. DeFazio, I did not see you. I apologize. We are going to get you

started in any event while we have got a few minutes left on this vote.

STATEMENT OF HON. PETER A. DEFAZIO, REPRESENTATIVE IN CONGRESS FROM THE STATE OF OREGON

Mr. DEFAZIO. Thank you, Mr. Chairman.

Chairman ARCHER. Welcome to the Committee. We will be pleased to receive your testimony.

Mr. DEFAZIO. Thank you, Mr. Chairman. I have a brief testimony, which I submitted for the record, and I will just depart from that a bit in some brief remarks.

Just by way of background, Mr. Chairman, I have a degree in gerontology and some significant experience more on the OASDI side of Social Security but have put a lot of time into this, both my professional career as a congressional staffer and now as a Member.

So, I looked at the system. I see tremendous merit and value in trying to extend the current system intact as much as possible, because I think it works quite well but meet the 75-year standard of the actuaries. So, I poured through all of the various proposals the actuaries have put out on some thought papers; dozens of them on ways to increase revenues, and I came up with a few standards. I didn't want to decrease benefits. I didn't want to increase retirement age over what is currently proposed, and I wanted also, if possible, to see a way to provide some tax relief, because, as you certainly know as Chairman, more than 40 percent of the working people in America pay more in FICA taxes than they do in income taxes to the Federal Government.

So, the proposal I have submitted does raise taxes, but it raises taxes only on people who earn over the current earnings limit of $72,600. I would lift the cap as was done with Medicare, and that picks up more than enough money to resolve the problem or almost enough money to resolve the problem, but what I also do is invest benefits for up to 40 percent of the surplus on the aggregate basis that has been talked about in some other plans, all along the model of the TRS Program, not in the fully individualized account basis. And between those two things, we would be well above what is needed for 75-year sufficiency.

But then what I would do to make the tax more progressive and relieve the burden on 95 percent of working Americans is exempt the first $4,000 of income on the employee side from FICA tax, although those benefits—that earnings would be attributed to their record, but I would pay for that out of the money we get by lifting the cap, and I would do a couple of other minor improvements dealing with beneficiaries age 85 and older. They are predominantly women, and they are in a much higher rate of poverty. I would boost their benefits as proposed by the actuaries, and I would provide five additional drop-out years for child care.

So, in summary, I propose something that would provide tax relief to 95 percent of wage-earning Americans; would stabilize Social Security and has been certified by the actuaries over 75 years, the actuaries' window; would also provide for the additional child care drop-out years and the older workers and essentially adopt sort of what I would consider to be a fair, flat-tax approach to Social Secu-

rity, which is you pay on all your earnings, and that is my proposal, Mr. Chairman. It is quite simple, and it would solve the problem.

[The prepared statement follows:]

Statement of Hon. Peter A. DeFazio, a Representative in Congress from the State of Oregon

Thank you, Mr. Chairman, Mr. Rangel and members of the committee for giving me the opportunity to testify today on my proposal to insure the future health of the Social Security program.

Social Security is one of the most popular and successful New Deal programs. It was created in 1935 and today provides essential retirement, survivors and disability benefits to 44 million Americans. Before Social Security was approved by Congress, more than one-half of America's elderly citizens lived in poverty.

Thanks to Social Security, fewer than 11 percent of today's seniors fall below the poverty line. Social Security provides more than half of the retirement income for two out of every three people over 65 years of age. Social Security benefits make up 90 percent or more of the income for about one out of three seniors.

It is important to understand that the Social Security Trust Fund is not bankrupt, nor will it be. According to the 1999 Social Security Trustees Report, Social Security is financially sound until at least 2034—35 years from now. Even if Congress does nothing to reform the program, Social Security will continue to provide 75 percent of current benefits for an additional 40 years—until the year 2073. With the relatively modest reforms that I am proposing, the Social Security system should be able to provide promised retirement benefits for many generations to come.

In fact, my proposal cuts taxes for 94% of working Americans, increases Social Security benefits for the most needy, and saves Social Security. My proposal amends the Social Security Act to restore 75 year solvency by:

- Providing a FICA payroll tax exemption for first $4,000 of income, cutting taxes for 94 percent of all workers. This exemption would cut Social Security taxes by more than 11 percent for an individual earning $35,000 a year. Approximately 40 percent of American taxpayers pay more in FICA taxes than they pay in federal income tax!
- Investing 40 percent of the future Social Security surplus in broadly indexed equity funds. Many state retirement plans already invest a portion of their surplus in the stock market.
- Making all earnings subject to payroll tax for both employer and employee beginning in 2000. Retain the cap for benefit calculations. This affects only those who earn more than $72,600 a year—less than 6 percent of wage earners.
- Increasing benefits at age 85 by 5 percent. Women over the age of 85 are more than twice as likely to live in poverty than men of the same age. There are more than twice as many women as men over the age of 85.
- Allowing up to 5 child-care drop-out years. Parents should not have reduced Social Security benefits because they chose to stay home to raise their children.

The Social Security program is the most successful government program ever undertaken. With these changes it can remain so. Thank you, Mr. Chairman, I would welcome questions from you or other members of the Committee.

Chairman ARCHER. Well, your explanation is brief and to the point, and the Chair appreciates that as we move into the afternoon.

Mr. Cardin, do you have any questions?

I think it is pretty clear what you are suggesting, and I thank you for going through this process, getting certified by Social Security, and appearing before us today.

Mr. DEFAZIO. Thank you, Mr. Chairman. I will look forward to your support. [Laughter.]

Chairman ARCHER. Well, we are going to have go through quite a deliberation before we get to there.

Mr. Nadler, do you want to go vote and then come back?

Mr. NADLER. Yes.

Chairman ARCHER. Very well. The Committee will stand in recess for an adequate period of time to vote and immediately—will you return right away, Mr. Nadler? Great, thank you.

[Recess.]

Mrs. JOHNSON of Connecticut [presiding]. The hearing will reconvene.

Mr. Nadler, it is a pleasure to have you.

STATEMENT OF HON. JERROLD NADLER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. NADLER. Thank you, Madam Chairperson. Thank you for the invitation to testify before the Committee.

I introduced H.R. 1043, legislation which has been pending before this Committee since March 9. This bill would make Social Security solvent for at least 75 years without raising the retirement age, without cutting benefits in any way, without shifting the risk onto individuals through private accounts funded by FICA taxes, and without raising tax rates.

The plan also does not adjust the CPI; it does not reduce COLAs; it does not force only State and local government employees into Social Security; it does not increase the benefit computation above 35 years; it does not cut benefits by adjusting the bend points; it does not cut benefits in any way. The plan does not rely on general fund transfers beyond an initial 15-year period, unlike the Archer-Shaw plan.

The bill has been scored by the Social Security actuaries as completely eliminating the long-range OASDI actuarial deficit. In fact, it would improve the long-range OASDI actuarial balance by an estimated 2.55 percent of taxable payroll, replacing the actuarial deficit of 2.07 percent under present law with a positive actuarial balance of 0.48 percent of taxable payroll.

In addition, at the end of the 75-year period, Social Security would remain strong. Some criticisms have been leveled at some other proposals by saying, "Yes, they would make the Social Security for 75 years, and then we would go broke in year 76." That is not the case with this bill. In fact, the trust fund ratio at the end of 75 years would then be 793 percent compared to its current 194 percent; that is the ratio of money in the trust fund toward annual payouts would be almost 8 to 1 at that point compared to a little under 2 to 1 now.

So, it has ongoing strength, and in fact will be as solvent as far into the future as we can see. The plan maintains Social Security is a guaranteed, lifelong, cost of living adjusted, defined benefit plan. That is the heart and soul of Social Security, and that is why I fought so hard to preserve the vital program.

So, how does this legislation work? Essentially, the plan follows and builds on the President's suggestion. The bill would transfer 62 percent of the projected budget surplus to the Social Security Trust Fund for a period of 15 years, not forever. It would provide for the investment of a portion of the funds in broad stock index funds and would raise but not eliminate the wage cap. It would raise it above the current $72,600.

The bill would implement the President's proposal to authorize the transfer of 62 percent of the projected budget surplus to the So-

cial Security for 15 years. It expresses this figure as a percent of taxable payroll and is not dependent on actual budget surpluses to materialize. If the economy does better than projected over the 15-year period, more funds would be allocated to Social Security. If the economy does worse, less funds would be transferred, and there would be correspondingly less pressure on other government spending.

The bill would create an independent Social Security Investment Oversight Board, members of which would have long staggered terms which would then hire several competing private managers to invest a portion of the trust fund in broad market index funds. Some people incorrectly describe this as government investment in the market. This is somewhat misleading. There would be no picking and choosing of stocks by the President, by Congress, or anyone else in government. The investments would follow a fixed formula and not the whims of some investment genius. No geniuses need apply for employment under this plan.

The investment is completely private and fully insulated from political influence by several layers of protection. Federal employees currently invest in the market through the Thrift Savings Plan. I am not aware of anyone who has suggested that Congress has tampered with the market due to this type of collective investment. In fact, several of the plans that include individual accounts have similar restrictions on investments which would essentially require the same type of protections to be included in their plans. Individuals would be severely restricted in their investment decisions and in some cases only allowed to invest in broad index funds approved by the government. Here, of course, the private investment managers would do the investing in the investment funds.

Many State and local governments currently invest up to 60 percent of their assets—of their pension assets in the stock market. This bill would authorize half of that amount and would prohibit investing more than 30 percent of total trust funds assets in the market. In order to extend the projected solvency of the Social Security system for 75 years, the bill would invest up to 30 percent of the funds of the trust fund surpluses in the market.

Keep in mind, under this legislation, most of Social Security's funding will still come from payroll taxes and interest on government bonds. The actuaries informed us that under current law, beginning in 2034, payroll taxes will be sufficient to cover 75 percent, roughly, of benefit payments. The other 25 percent of payments would have to come from the trust fund. A maximum of 30 percent of the trust fund under my bill would be invested in the market. Thirty percent times 25 percent is 7.5 percent. In others words, funds for only 7.5 percent of benefits could be at any market risk at all. It has been estimated that if the market collapsed by 50 percent, the ability of Social Security to pay benefits would be reduced by less than 2 percent at worst. So, the risk to the system under this bill is quite small.

The real difference between this approach and the various private account approaches is twofold. One, this approach is a lower cost, more efficient, and more prudent way of increasing the rate of return on Social Security assets. There are staggering administrative costs for setting up 150 million individual accounts and

tracking them year by year for 40 or 45 years with allowances made for annual adjustments to each account. This is an incredible burden that is completely unnecessary and wasteful.

The second difference is that this bill retains Social Security as a guaranteed benefits plan, whereas the various market proposals—or most of the various individual account proposals make part or all of your benefits depending on how well your individual account did in the market, and even if on average the market did very well and on average individual plans did very well, many millions would be below average and would not do very well, and it would subject millions of Americans to market risk. This bill would not.

This legislation, starting in fiscal year 2000, would incrementally increase the cap on taxable wages above the current $72,600. Currently, 86 percent of all wages are subject to FICA contributions. This has slipped in recent years from the historic 90 percent because of the dramatic rise in the disparity of wage levels in our society.

The Social Security actuaries inform us that 93 percent of wage earners earn less than the current cap, and, therefore, pay FICA taxes on all their earnings. About 7 percent of all wage earners do not pay FICA taxes on all of their income. This bill would require the wealthiest 7 percent to pay the same FICA tax rate on a slightly greater portion of their earnings. It would not eliminate the cap completely, unlike Mr. DeFazio's plan. To ensure fairness, these individual Social Security benefits would increase, as well, to reflect the higher cap. Keep in mind, I would also point out this simply would restore the percentage of wages subject to the tax to 90 percent and to do that would only impact on 7 percent of wage earners.

This plan makes the system act solvent even under the actuaries' extremely pessimistic intermediate assumptions. Many of their predictions are questionable especially of the fact they predict economic growth to average 2.0 percent for the years 2000 to 2007 as they have for the last 5 years, despite economic growth rates of 3.4 percent in 1996, 3.9 percent in 1997, and 3.9 percent in 1998, and slightly better than 4 percent so far this year. They then predict economic growth to take a significant downturn to 1.4 percent from 2020 to 2040 and 1.3 percent from 2050 to 2070. The further predict the economy will do even worse than after that. To put these numbers in some perspective, we should know the economic growth rate was 4.6 percent from 1960 to 1964, 5.4 percent in 1976, 7 percent in 1984, and 3.25 percent for the last 37 years. So, H.R. 1043 restores solvency even in light of these extremely pessimistic projections. If the actuaries are wrong and the economy does better than they presume, as I predict it will, Social Security will be in even better shape, and we will have plenty of money to increase benefits in various ways or to reduce the tax rate.

The legislation I have proposed is supported by the Older Women's League, The 2030 Center, the Americans for Democratic Action, among others. I would commend it to the consideration of the Committee. And, again, to summarize, unlike most of the other proposals, it puts no market risk on any individual whatsoever, calls for no benefit reductions, no increase in the retirement age,

does not mortgage the budget surpluses forever as the Archer-Shaw plan would do, calls simply for 62 percent of the budget surplus for 15 years to be put into the trust fund, calls for investment by private sector investment managers of up to 30 percent of trust fund surpluses in the stock market, and would somewhat raise the wage cap and would thereby make the system solvent, not only for 75 years but for as far into the future as we can see and would in fact give us a ratio, a payout ratio 75 years from now of almost 8 to 1 compared to today's less than 2 to 1.

[The prepared statement follows:]

Statement of Hon. Jerrold Nadler, a Representative in Congress from the State of New York

Thank you, Mr. Chairman, for your invitation to testify before this committee.

I have introduced H.R. 1043, legislation which has been pending before this committee in legislative form since March 9. This bill will make Social Security solvent for at least seventy five years without raising the retirement age, without cutting benefits, without shifting the risk onto individuals through private accounts funded by FICA taxes, and without raising tax rates.

This plan also does not adjust the CPI, does not force all new state and local government employees into Social Security, does not increase the benefit computation period above 35 years, and does not cut benefits by adjusting the bend points. This plan does not rely on general fund transfers beyond an initial fifteen year period.

It has been scored by the Social Security Actuaries as completely eliminating the long-range OASDI actuarial deficit. In fact, it would improve the long-range OASDI actuarial balance by an estimated 2.55 percent of taxable payroll, replacing the actuarial deficit of 2.07 percent under present law with an positive actuarial balance of 0.48 percent of taxable payroll.

In addition, at the end of the seventy five year period, Social Security would remain strong. In fact, the trust fund ratio would then be 793 percent. The current trust fund ratio is approximately 194 percent.

This plan maintains Social Security as a guaranteed, life-long, cost-of-living-adjusted, defined benefit plan. That is the heart and soul of Social Security, and that is why I have fought so hard to preserve this vital program.

So, how does this legislation work?

Essentially, the bill would transfer 62 percent of the projected budget surplus to the Social Security Trust Fund for a period of 15 years, would provide for the investment of a portion of the funds in broad stock index funds, and would raise the wage cap above the current $72,600.

Surplus Transfer.

The bill would implement the President's proposal to authorize the transfer of 62 percent of the projected budget surplus to the Social Security Trust Fund for a period of 15 years. It expresses this figure as a percent of taxable payroll, and is not dependent on actual budget surpluses to materialize. If the economy does better than predicted over the fifteen year period, more funds would be allocated to Social Security. If the economy does worse, less funds would be transferred, and there would be correspondingly less pressure on other government spending.

The Independent Social Security Investment Oversight Board.

The bill would create the Independent Social Security Investment Oversight Board—members of which would have long, staggered terms—which would then hire several competing private managers to invest small portions of the Trust Fund in broad index funds which track the market based on a fixed formula. Some people incorrectly describe this as "government investment in the market." This is terribly misleading. There would be no picking and choosing of stocks by the President, Congress, or anyone else in government. The investments would follow a fixed formula and not the whims of some investment genius. No geniuses need apply under this plan.

The investment is completely private and fully insulated from political influence by several layers of protection. Federal employees currently invest in the market through the Thrift Savings Plan. I am not aware of anyone who has accused Congress of tampering with the market due to this type of collective investment. In fact, several of the plans that include individual accounts have similar restrictions on in-

vestments which would essentially require the same type of protections to be included in their plans. Individuals would be severely restricted in their investment decisions and in some cases only allowed to invest in broad index funds approved by the government.

Many state and local governments invest up to 60% of their assets in the stock market. This bill would authorize half of that amount and would prohibit investing more than 30% of total Trust Fund assets in the market. In order to extend the projected solvency of the Social Security system for 75 years, the bill invests a larger, but still prudent, amount of the Trust Funds in index funds than the President's proposal which extends the projected solvency for 56 years.

Keep in mind, under this legislation most of Social Security's funding will still come from payroll taxes and interest from government bonds. The Actuaries inform us that under current law, beginning in 2034, payroll taxes will be sufficient to cover 75 percent of benefit payments. The other 25% will have to come from the Trust Fund. A maximum of 30% of the Trust Fund would be invested in the market. 30% of 25% is 7½%. In other words, funds for only 7½% of benefits could be at any market risk at all. It has been estimated that if the market collapsed by 50 percent, the ability of Social Security to pay benefits would be reduced by only 2%. So the risk to the system, under this bill, is quite small.

The real difference between this approach and private accounts is that this approach is a lower cost, more efficient, and more prudent way of increasing the rate of return on Social Security assets. There are staggering administrative costs for setting up 150 million individual accounts and tracking them year by year for forty years with allowances made for annual adjustments to each account. This is an incredible burden that is completely unnecessary and wasteful.

Increase, and then index, the cap on taxable wages.

This legislation, starting in fiscal year 2000, also incrementally increases the cap on taxable wages above the current $72,600. Currently, approximately 86% of all wages are subject to FICA contributions. This has slipped in recent years from the historic 90% due to the dramatic rise in disparity of wages. The Social Security Actuaries inform us that 93% percent of wage earners earn less than the current cap, and, therefore, pay FICA taxes on all of their earnings. About 7% of wage earners do not pay FICA taxes on all of their income. My bill would require the wealthiest 7% to pay the same FICA tax rate on a slightly greater portion of their earnings. It would not eliminate the cap completely. To ensure fairness, these individuals' Social Security benefit levels would increase as well.

Keep in mind this plan makes the system solvent even under the Actuaries extremely pessimistic intermediate assumptions. Many of their predictions are questionable especially the fact that they predict economic growth to average 2.0 for the years 2000–2007, despite economic growth of 3.4 percent in 1996, 3.9 percent in 1997, and 3.9 percent in 1998. They then predict economic growth to take a significant downturn to average 1.4 from 2020–2040 and 1.3 percent in 2050–2070. They further predict that the economy will do even worse after that. To put these numbers in some perspective the economic growth rate was 4.6 percent from 1960–64, 5.4 percent in 1976, 7.0 percent in 1984. So H.R. 1043 restores solvency even in light of these extremely pessimistic predictions. If the Actuaries are wrong, and the economy does better than predicted, Social Security will be in even better shape.

The legislation that I have proposed, H.R. 1043, is also supported by Americans for Democratic Action, OWL (the Older Women's League), and the 2030 Center. A large national organization, a women's organization, and an organization primarily concerned with protecting the interests of young people.

Mrs. JOHNSON of Connecticut. Well, thank you very much for your testimony and for all the thought that you have put into meeting this challenge.

I do hope that you don't loosely go around describing that other plans put people at risk of the market.

Mr. NADLER. Some do, and that is what I said.

Mrs. JOHNSON of Connecticut. For instance, the Archer-Shaw plan does guarantee the benefit, so the risk is taken by the government, not by the individuals.

Mr. NADLER. Well, in the Archer—I said some of other plans; I didn't say all other plans.

Mrs. JOHNSON of Connecticut. I have not noticed that many of the plans didn't guarantee the benefit.

Mr. NADLER. Well, most of the privatization proposals—not the Archer-Shaw plan and I don't think the Kolbe-Stenholm plan—but most of the privatization plans that have been around essentially say in one form or another that you are going to take 2 percent or 4 percent or 6 percent, depending on the plan, of the 12.4 percent FICA tax; you are going to divert it into market investments; you will be——

Mrs. JOHNSON of Connecticut. Well, I think that may have been the loose idea at the beginning, but I am not aware of a single plan that has been introduced that actually does expose people to market rates and doesn't guarantee the benefits that Social Security currently——

Mr. NADLER. I will look at that again, but I think that some of those plans, in fact, many of them do.

I would also point out that——

Mrs. JOHNSON of Connecticut. Well, many of them—don't use many——

Mr. NADLER. Well, some of them.

Mrs. JOHNSON of Connecticut. It is very important if we are ever going to get through this.

Mr. NADLER. I will look at that again, but it is certainly true of some of them. It is certainly true of the some them.

Mrs. JOHNSON of Connecticut. Well, we will see if some of them say that.

Mr. NADLER. And whether it is many or some, I won't quibble now. My impression was that it was true of——

Mrs. JOHNSON of Connecticut. Of those that have been written up and introduced, that is the universe of plans this Committee is concerned with——

Mr. NADLER. OK.

Mrs. JOHNSON of Connecticut [continuing]. And that have been certified to be effective over 75 years, and if some of those do, then fine, but I am personally not aware, and the ones I am aware of are very committed. So, I think it is very important not to get people involved in the fear factor being subject to the market when in most of these plans, the government is going to take that risk.

Let me ask you, though, as one who was early very interested in investing some of the Social Security surplus in the market, I am interested in your plan, but I don't see that is accomplishes the level of insulation that would have concerned Chairman Greenspan.

Mr. NADLER. Well, I think it insulates it as much as it can be insulated and I think quite effectively in the following manner: first, an investment board would be created, an independent board, consisting of Presidential appointments confirmed by the Senate with overlapping very long terms, 14-year terms, so as not to be responsible or responsive to any particular administration; second of all, the only two things they would do, that is that board would do, is not to pick and choose stocks; they would simply decide three things. One, how much in gross dollar terms should be invested in

the market this year and how much next year? Two, how many pieces should we break that amount into? Let us say we are going to invest $1 billion in the market this year. Should we break into five portions of $200 million or two portions of $500 million? And, three, for each of those portions, whom should we hire among private investment managers to manage that? So, all they will decide is——

Mrs. JOHNSON of Connecticut. With all due respect, what would prevent Congress from passing legislation——

Mr. NADLER. I am sorry?

Mrs. JOHNSON of Connecticut. What would prevent Congress from passing legislation like many States prevented past legislation during earlier decades to since prohibit those fund managers from investing money in South Africa or whatever is the thing at the time?

Mr. NADLER. Well, the third thing—you didn't let me come to the third thing—the third thing is that the legislation would mandate that the only thing the fund managers could invest in are market index funds, so they can't invest in any company, whether it has investments in South Africa or anywhere else. The index fund that they invest in might have some share, but they can only invest in index funds, and since they can only choose index funds, then the legislation also—that track the market.

Mrs. JOHNSON of Connecticut. All right. I do appreciate that. I am not sure that you can bind future Congress' to not legislate that they can't solicit any index fund that invests in South Africa.

Mr. NADLER. Well, let me answer that question. I will answer it twofold. Number one, there is no way that any plan can prevent a future Congress from doing anything it wants; that is constitutional.

Mrs. JOHNSON of Connecticut. Right.

Mr. NADLER. And I would submit that the experience that we have with the Thrift Savings Plan—this is modeled on the Thrift Savings Plan as are elements of some of the other bills in terms of some of their private investments. I don't think we have had that problem.

But I would submit one other thing. I don't think Congress is likely to do that. To do that, they would have to upend the entire statutory scheme here, and I would say one further thing, and I will be very blunt: if some tremendous social movement arose in the future—if Hitler were reborn, took over, the Nazis were running Germany again, and some tremendous moral movement came up in this country that says don't invest in Nazis and Congress were to succumb to that, so what?

Mrs. JOHNSON of Connecticut. Thank you.

Mr. NADLER. I don't think that is so terrible.

Mrs. JOHNSON of Connecticut. Let me recognize the Chairman.

Chairman ARCHER [presiding]. I have no questions other than to compliment you for coming and presenting your plan, and it is a full plan that does have the certification that it will save Social Security for 75 years. There are many who think that is not important. Frankly, I think it ought to be more than 75 years as life expectancy has gone up to above 80, and you have given thought to it, and we appreciate your testimony. I have no questions.

Mr. NADLER. Well, I appreciate your comment. Let me just mention, you didn't hear—you weren't here—to say that this bill—the reason I am saying this is to allude to what you said a moment ago. There has been criticism made of some suggestions that 75 years is not enough; that if you have 75-year solvency but the plan goes broke and you are 76, that maybe we ought to do a little better than that. This plan not only has 75-year solvency but achieves a ratio of trust fund assets to payout of 793 percent or almost 8 to 1 75 years down the road. So, in fact, it is solvent as far into the future as we can see.

Chairman ARCHER. Sure, it gets better and better and better, and that part of it is, in my opinion, very, very good. I have no questions.

Mr. Rangel.

Mr. RANGEL. Thank you, Mr. Chairman. Jerry, why didn't you remove the cap altogether?

Mr. NADLER. I chose not to remove the cap altogether for several reasons. First of all, I made the basic decision—and let me just say one other thing: this bill was not designed to pass exactly as is. This bill was introduced several months ago. It was the plan that got actuarial certification. I believe it was designed to show that you can in fact achieve actuarial solvency over the 75 years without subjecting anybody to individual market risk, without reducing benefits, without increasing the retirement age, and without increasing tax rates. That was the purpose of it. There are a lot of different variants on it. In on sense, Mr. DeFazio's bill is a variant; it is the same basic approach.

I chose, in this bill, not to eliminate the cap for several reasons. One, right now, benefits are to a large extent proportional to contributions. There are different bend points in the rates, as you know, but, basically, the higher your contribution, the higher the benefit. If you eliminated the cap completely, either you would have for a few people very sky high outrageous benefits which might conceivably lessen the political support for the system at some future point in time or maybe increase pressures for calling for means testing the system.

Alternatively, you could, as Mr. DeFazio would, divorce, simply say we are raising the cap on contributions but not on benefits, and then it would make that—I don't think we should remove the nexus between contributions and benefits. It becomes, then, a straight tax as opposed to contribution, and it is a fundamental change in the system, and I think it raises a lot of political problems in terms of support in the future.

Third, as a straight political judgment, I thought it less likely that we would ever pass something like that in Congress than simply raising the cap, and the figure I chose to raise the cap to is simple. It was based on—it had, not traditionally, but had often been in the past capturing 90 percent of wages to be FICA taxed, and that was sufficient with the other things to what we needed to do.

Mr. RANGEL. What was your thinking legislatively, economically, or politically as to attaching the private sector investment to this bill?

Mr. NADLER. Well, I think it is an excellent idea. I mean, if anyone has money—if you won the lottery tomorrow and you got $10

million and you went to an advisor to ask him how to invest it, anybody would tell you "Diversify your portfolio." That is true of anything, whether it is a State pension fund or a Social Security fund or a private account or private portfolio. You always want to diversify your portfolio to minimize risk and to maximize yield and to get a good balance of that.

Now, traditionally, Social Security didn't do that for a very simple reason. When Social Security was conceived and until 1983 when the system was changed deliberately to build up the trust fund to anticipate the baby boomers, there rarely were—there weren't expected to be sizable amounts of money in the trust fund. There was a float from year to year. There never was an expectation that we are going to have a lot of money, so you might as well just put it into the safest investment—Government bonds, and so forth. But now that you are building up huge amounts, you should get a higher yield than on Treasury bonds.

Now, the stock market over long periods of time does increase faster. Now, there are periods of downturn which tend to be 20-year periods, but over any long period of time, you do better with an investment in the stock market than you do in bonds or in Treasury bonds. So, we should take advantage of that.

Now, I did not like the private investment system, because under some—in deference to the gentlelady from Connecticut—under some private investment plans, you place market risk on individuals, and you turn Social Security from defined benefit to a defined contribution program, which I wouldn't want to do, and, in any event, you get a tremendous—you pay a tremendous price in terms of efficiency and administrative costs and under some plans in terms of transition costs. So, we eliminate all of this. But I think investing a reasonable proportion of the market is a good thing to do even if you didn't need to do it to get a big—even if you didn't need to do it, it is an intelligent thing to do.

Mr. RANGEL. Thank you. You have done a very good job with this bill. We appreciate your efforts.

Mr. NADLER. Thank you.

Chairman ARCHER. Thank you for your presentation, Mr. Nadler.

Mr. NADLER. Thank you.

Chairman ARCHER. And thank you for your patience in waiting your turn.

Our next witness is scheduled to be Mr. Smith. Is Mr. Smith available?

If not, our next witness is Mr. Sanford. Is Mr. Sanford available?

Well, the Committee will stand in recess for 5 minutes. If Mr. Sanford gets here by then, then we will be pleased to hear his testimony.

[Recess.]

Chairman ARCHER. Mr. Sanford, welcome.

STATEMENT OF HON. MARSHALL "MARK" SANFORD, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF SOUTH CAROLINA

Mr. SANFORD. Thank you, sir.

Chairman ARCHER. We are prepared to receive your testimony. I apologize to you for having kept you waiting for such a long pe-

riod of time, but we really don't control that, as you know, but we are glad to have you before us now, and we would be pleased to hear from you.

Mr. SANFORD. I thank you, sir. First of all, I would say thank you very much for holding this hearing to you, to Mr. Foley, to others on the Committee, for actually stepping out and talking about this issue that has needed a lot of talk for quite some time.

I would say that we have, as you know, got a number of different bills related to Social Security, but this latest bill and the one that you see featured in your write-up is basically a compromise bill. It is a political bill, and at the core it is about one thing, and that is about rebating the entire Social Security balance back to individuals who would then begin their own personal Social Security account, and it would begin to create what Greenspan talked about and that is a real firewall between Social Security balances and political forces in Washington, DC.

I think that the bill represents a compromise in that it is an amalgamation of a number of different ideas. It incorporates what Moynihan had talked about. Moynihan had talked about—I guess Kerrey and Moynihan—had talked about the idea that the tax rate right now is more than we need. The FICA tax is more than we need in Washington, and, therefore, their proposal has actually cut the tax rate, as we know. We don't do that but instead rebate that surplus back to the individual.

It incorporates the idea that the President talked about which was the idea of a refundable tax credit. Instead of lowering the rate, this bill simply issues to folks a refundable tax credit that begins to build a Social Security balance in their personal account.

It incorporates your idea, sir, the Archer-Shaw idea of using general fund revenue to basically help through a transition. You know, I think you are absolutely, 100 percent right in this idea, because if you look around the globe at any of the different proposals that have worked in transitioning from a collective system run by the power of the State to a series of individual accounts, in every case, general fund revenues have been used.

It uses some of the ideas of Kolbe-Stenholm—and I listened to some of their testimony earlier—on basically small—we take a number of their changes and refine—basically, we use just a few of them—but, nonetheless, structure reform to existing Social Security, and, most of all, what this simple idea takes advantage of is the idea of personal accounts, and I think that is the one common denominator that to a greater or lesser extent you have heard in all the different reform proposals.

So, it is, again, a small bill. It is a reform bill, not so much on Social Security as a whole, but simply on trying to lock down Social Security surpluses so that they stay for Social Security. I would liken it to a super lockbox, if you will. As we all know, last year, Washington, through the unified budget, borrowed $100 billion from Social Security, and they did so without a lot of fanfare. I mean, when I talk to folks back home in my district and bring up the $100 billion of borrowing, most folks don't even know about it, and those that do didn't exactly march on Washington. I mean, they may have written a letter to their Congressman or Senator, but that was about it. And if that same money had been housed

in some of form of personal account across this country and then Washington reached in and attempted to borrow that same $100 billion, I mean, you would have a revolution on your hands. I don't know about you, Mr. Chairman, but I know the folks back in my district, the idea of saying, "Well, we came up short. Your pro rata share of this will be $743.27" would not go over real well with folks in my district. And, so it really creates that firewall that I think that we are all looking for. As we all know, as well, the omnibus bill of last year, over $20 billion borrowed from Social Security. Would that have been possible with personal accounts? In the supplemental just a couple of weeks ago, would that have been possible if the money had been in personal accounts? So, it really, more than anything else, is a bill about locking down Social Security surpluses more than it is a bill about reform of Social Security.

Two, I would say that it relies on the "bird in the hand" theory. What the bill really does is it prefunds Social Security. In other words, since more money is coming in each year in FICA taxes than is currently needed by Social Security, what it says is, "All right, would you like your money now?" Now, if history is any indicator based on what has happened in other parts of the globe, people would say, "Yes," and by doing so—and I think this is where there is something about this bill that does work—by doing so, since it already had been prefunded, that piece of their Social Security, that means it will give up that part of traditional Social Security. And that voluntary reduction of future reliability I think is one of the real strong pluses, because—I heard your testimony with Kolbe-Stenholm—one of the problems we get into politically is when you begin looking at a lot of reform or cut of current benefit, even if it is a hypothetical benefit, but nonetheless it is a stated benefit, if you look at that, you have real political problems with that. This would be a voluntary reduction of that benefit, because people would be prepaid that benefit.

Last thing that I would just touch on for 2 seconds would be that it allows for real wealth creation. Again, this is a theme that has been constant to all the different Social Security proposals that we have talked about. But in these little accounts—and I am just going to use a 5-percent rate of return. You could use 3 percent; you could use 2 percent; you pick the rate, but just to give you an idea of numbers, based on projected Social Security surpluses, these nominal numbers by 2014 would amount to basically $6 trillion and $3.8 trillion of real wealth would be created. Again, if you take it out a little bit further to 2034, you would be looking at about $40 trillion in nominal, about $10.8 trillion in real by 2034 in individuals' personal accounts.

I think that that—and, again, to give you an idea of relative scale, the New York Stock Exchange, as we all probably know, is about $11.3 trillion in size. The value of all exchanges globally is right a hair below $30 trillion in size, so you are talking about a lot of money that would be out there in the markets, and that goes straight to the point that I guess Marty Felstein and others have emphasized, which is there is real value to the economy if you get that money in individual accounts, in terms of asset allocation or in terms of where the money would go. It would go to, whether it is a Corning plant or whether it is a chainsaw plant in my district

or whether it is a sugar factory down in Mark Foley's district—in other words, it could go to a lot of other places that are probably a lot more productive in the American economy than the way that that money might be allocated here in Washington.

So, that would be at least a thumbnail sketch of sort of what the bill does, and I would open for questions.

[The prepared statement follows:]

Statement of Hon. Marshall "Mark" Sanford, a Representative in Congress from the State of South Carolina

Thank you Mr. Chairman and members of the committee for allowing me the chance to talk about my Social Security reform proposal.

My plan is designed as a compromise approach, borrowing from provisions of other leading reforms. At its core, it is a rebate of the entire Social Security surplus each and every year.

My proposal incorporates a number of the structural reforms from the Kolbe-Stenholm plan, such as adjusting early retirement benefits and benefits for higher-income workers. Like Archer-Shaw, my plan utilizes general revenues to soften the amount of structural reform necessary to achieve actuarial solvency. I also include the President's notion of automatic refundable tax credits from his USA accounts proposal. And from Sen. Moynihan's approach and the lock box, my proposal is based on the premise that the government should not be taking in more than it needs in a given year.

Folks back home tell me that a lock box is great, but unfortunately, Congress can still dip into Social Security surpluses. What we need is a "Super Lock Box" personal retirement accounts. Such an approach has the added benefit of paying down a portion of the program's expected $19 trillion shortfall of the next 75 years.

First, the plan would provide a system of personal retirement accounts (PRAs) that, for the first time, would enable workers to own and control their retirement security. For years, Americans have mistakenly believed that their Social Security numbers are the numbers on their retirement accounts. Under this plan, that actually would be the case.

The bill would allow each working American to receive his or her share of the Social Security surplus each year, directly deposited into individuals' PRA. How would this work? Look at last year.

In 1998, Social Security ran a $100 billion surplus. Washington spent $30 billion, and the remaining $70 billion paid down existing federal debt. Not a penny was used to pay for Social Security reform.

Under my approach, however, Social Security's $100 billion surplus would have been rebated back to Americans' PRAs. Every worker would have had about one-fourth of what he paid in Social Security taxes given back to him by the Treasury Department.

If last year's Social Security surplus had been deposited in personal retirement accounts across the nation, there would have been no way to "borrow" that $100 billion. Imagine if we all had to go to every American and tell them we needed their pro rata share, paid for out of the PRAs, on the Defense Supplemental. There would have been a nationwide march on Washington. And that's the way it should be. We need a firewall.

The need for a firewall became even more apparent just last month. During the Defense Supplemental, Congress had a chance to set aside money by cutting non-defense discretionary spending by a modest 5% to pay for the additional appropriations. Only 96 Republicans and 5 Democrats voted for the amendment offered by Rep. Tom Coburn, Rep. Pat Toomey, and myself.

Why was there no major protest that we spent $13 billion of the Social Security surplus? Because people had no real connection to that money. When Congress and the President spent $30 billion of the Social Security surplus last year, some people were angry enough to call or write their Congressmen and Senators, but that was the extent of it.

But if we rebate the surplus every year, we create the necessary firewall and we reduce Social Security's unfunded liability. Money rebated to the accounts would be considered early payment of future Social Security benefits, which would reduce the program's future financial obligations. Because the program is running surpluses now, it is common sense to provide for future benefits while we can. Folks in general prefer "a bird in the hand." Even folks in my district who are in their forties and fifties don't believe they are going to get Social Security.

Although the Lock Box is a great first step toward meaningful reform, we cannot stop there. Even if we stay faithful to the pledge of using all the money in the lock box for debt reduction—and that's a big if with Washington's fiscal discipline—we would still have to run the debt held by the public up by $8.3 trillion by 2034. (see chart) And that would do nothing to improve the poor rate of return people get out of Social Security.

But by counting the rebates as early payment of future benefits, the unfunded liability of Social Security is reduced. Here's how this works on an individual level. When people retire, the Social Security Administration will run a few calculations. First, they will determine how much money a person has received in government rebates to their accounts, adjusted to present value figures using the long-term U.S. bond rate. Second, they calculate the present value of all expected future benefits from Social Security. Peoples' benefits will be offset proportionally, the value of the rebates divided by the value of the expected benefits.

For example, Mary works full-time for $8 per hour over a 40-year career. By retirement, she has had $40,000 (in real terms) in rebates to her account over the years and the present value of expected Social Security benefits is $140,000. Her monthly payments would have been $700 per month in today's dollars, but that would be offset to $500 per month since she had already received 28.5% of her benefits in the form of rebates. The value of her account, assuming a conservative 5.5% real rate of return, would be $75,000, or enough to purchase a lifetime annuity worth $375. In other words, the personal account would increase her benefits by 25% with just a modest rate of return.

If the accounts earn just 8% nominally or under 5% after inflation, workers would own a total of $6 trillion, or $3.8 trillion in real terms, in assets by 2014, according to Scott Hodge of Citizens for a Sound Economy. Mr. Hodge also found that by 2034, the aggregate value of the accounts will grow exponentially to $40 trillion, or $10.8 trillion in today's dollars, and that's not even factoring in any voluntary additional contributions. Just to put those figures in perspective, the total market capitalization of the New York Stock Exchange is $11.3 trillion. The total market capitalization of all domestic exchanges is $28.8 trillion.

The second main aspect of my approach is the administrative structure. My philosophy is that we should not reinvent the wheel. America has the most well-developed capital markets in the world, and two of the great successes in our marketplace are 401(k) retirement savings plans and individual retirement accounts (IRAs).

43% of American workers have 401(k)s. People like them for many reasons, some of which are individual ownership, money growth without taxation, monthly statements and the stringent guidelines on investment.

Personal Social Security accounts would work the same way. Employees who have 401(k) accounts could establish sister accounts provided their employer wants to offer the option. Those who do not have 401(k)s would start an account at a national financial institution, a nonprofit, a union, or at the local bank.

Like in 401(k) plans, the worker could not withdraw the money before retirement or speculate on hot stock tips from a crazy brother-in-law. The investment choices would be diversified but limited and managed by a private financial manager—not a government bureaucrat.

Any group that can get Securities Exchange Commission approval, which would rest on factors such as capital structure and liquidity, can become a Social Security plan trustee. Approved plan trustees could offer multiple plans and would select 5–15 look-through investment options for each plan.

All plans outside of employer plans would be required to contain a minimum of these three options: 1) a broad-based stock index fund, 2) a broad-based bond index fund, and 3) Treasury securities. So if a worker wants to invest solely in Treasury securities, he can. This allows that every worker will have a number of very low-cost investment options available to him.

Workers would have guidance in making their investment decisions, since the same education and disclosure requirements from 401(k)s would apply to Social Security accounts. But in the electronic age, costs on these provisions will be relatively low.

The administrative structure of accounts in my approach has specifically been designed to minimize costs. Using the 401(k) model affords you efficiency savings by having many uniform accounts in a particular plan, with the only difference between accounts being asset allocation. By stripping out the loan and access provisions common in 401(k)s and having only large aggregate deposits, the PRAs will be significantly less expensive than 401(k)s.

The third main component of my proposal is its progressivity. My plan is quite progressive for 4 main reasons. 1) It lessens the link between longevity and benefits,

2) people on the low-end economically would come out far better than under the current system, 3) automatic refundable tax credits that would supplement Social Security rebates for low-income workers, and 4) administrative fees for low-wage workers would be paid for by the government.

Everyone agrees that lower-income folks must be protected no matter what reform is enacted. Providing PRAs that don't force the purchase of an annuity automatically makes Social Security more progressive by decreasing the relationship between life expectancy and benefits received. According to "Health, United States, 1998," blacks have the shortest life spans among all racial demographics, and there is a straight-line correlation between socio-economic status and life expectancy.

Beyond real wealth creation in PRAs, the best way to protect lower-earning career workers without distorting their normal investment incentives is to not offset their monthly government benefit changes, while still allowing them to keep all the money in their accounts.

My plan specifies that people with average indexed monthly earnings of $650 or less, who make up about 20% of the career work force, would receive no offset in their monthly benefit checks based on rebates to their accounts. The normal benefit offset of rebates counting as early payment of future benefits would be phased in between average indexed monthly earnings of $650 and $1150. An AIME of $1150 is about the 35th percentile of the career work force.

The third thing we do for low-income workers is incorporate the President's USA accounts concept by having an automatic refundable tax credit to supplement the Social Security rebate. Each of the first two years that a worker earning less than $25,000 has a PRA, he or she would receive up to a $300 automatic refundable tax credit. This helps these folks to build and create real wealth very quickly.

The fourth and final thing we do for low-wage earners is we use general revenues, stated as a permanent budget line item, to pay the administrative fees for workers earning less than $20,000 per year. This way, there is no chance that small accounts could be eaten up by administrative fees.

My plan also has a special protection for women. At retirement, the higher earner of a married couple must purchase a survivor's annuity to ensure that should the higher earner die first, that the surviving spouse would be in no worse condition than under current law. In other words, the offsetted benefit plus the survivor's annuity would have to at least equal current law survivor's insurance benefits. This provision ensures that widows will not be in a position to outlive her assets in her later, and vulnerable, years.

The most important aspect of my proposal, which greatly benefits lower-income Americans as well as farmers and small businesses, is the real wealth creation that can be passed on to one's children and grandchildren. The lowest 40% economically in our country retire in net debt, not net equity. Instead of thinking about the inheritance to be handed down, they are worrying about how to pass on as little debt as possible. That should not be the case.

Farmers and small businessmen face a similar plight. The only investments that they make throughout their careers is for new capital equipment, not stocks and bonds. They are asset rich and cash poor. Our bill would allow them to retire asset rich and cash rich. Everyone pays Social Security taxes, so why not use the one funding vehicle for retirement savings that everyone can take advantage of?

On the financing of the transition to a partially pre-funded system, my plan uses a combination of modest structural reforms and general revenues transfers. My proposal has three structural reforms: 1) reducing early retirement benefits by about 1.6% per year of early retirement, 2) gradually reducing the 15% bend point, which affects the top 30% of lifetime earners, to 10% between 2009 and 2028, and 3) eliminating the 11-year hiatus during which the retirement age does not increase by two months per year from age 66 to 67.

Reducing the early retirement benefits in this manner more accurately reflects the budgetary impact of retiring early. Under current law, early retirement benefits are actuarially reduced so that on the whole people who retire early get the same amount they would have had they retired at the normal age. However, those calculations do not consider the fact that people who retire early are not paying Social Security taxes into the system. The proposed adjustments would account for that lack of FICA contributions.

Some might complain that my changes in early retirement benefits harm lower-income workers. But the reason many lower-income workers claim early retirement is because they have no net wealth from which to draw to pay for the high costs of growing old. My bill addresses this problem by allowing people penalty-free access to their accounts starting at age 62, without having to declare retirement to do so.

Reducing the 15% bend point down to 10% over a 20-year period is a reform that results in up to a 7% cut in benefits for the top 30% of average lifetime income earn-

ers. Less than 10% of retirees after 2028 would even lose 7% of benefits. Everyone else who is affected, but did not earn the maximum salary subject to FICA taxes, would only see their benefits reduced between one and 7 percent.

The third structural reform is achieved by having the retirement age reach 67 years old just a little sooner than it does under current law, 2016 as opposed to 2027. My plan does this by adjusting the retirement age table, eliminating the eleven-year period after the retirement age reaches 66 where the retirement age does not increase by two months per year.

The general revenues financing comes as a part of the rebate itself. Because my plan is not a true carve-out, the trust fund continues to grow at the same time as the accounts are growing from annual contributions. The accounts receive rebates totaling the amount of the total operating surplus (cash plus interest) of Social Security. The trust fund, in essence, becomes the marker by which we determine how much general revenues is owed to the personal accounts in order to make the transition to a partially pre-funded system.

Using general revenues to transition to a pre-funded system based on real wealth creation for all working Americans that can be passed on to children and grandchildren is not a new concept. Every country that has moved from a pay-as-you-go public structure to a private, pre-funded system has used general revenues to pay for the unfunded liability that had already been incurred. Just for the people currently in the work force, Social Security will lack the tax revenue funding for $9 trillion worth of promised benefits during their retirement years. As long as general revenues are used solely toward the goal of changing the nature of Social Security and promoting real wealth creation, then such use of general revenues can be effective and productive.

As for Disability Insurance, it is a program ripe for reform. However, now is not the time or place to address those issues. Washington moves in baby steps, and we need to focus on the retirement side of Social Security this year. By the same token, we can't just reform the retirement side of Social Security but allow disability insurance to gobble up more and more money from retirement funding.

The best approach, I think, is to cap DI at 1.8% of payroll from FICA taxes and condition that any extra funding come from cuts in domestic discretionary spending in general revenues. This will force a future Congress to deal with the issue in a way that could not possibly be done this year.

Using ideas from both sides of the aisle, I believe that my plan is a true compromise approach that can appeal to both Democrats and Republicans. Combining some of the structural reforms of Kolbe-Stenholm, the idea of general revenues financing of Archer-Shaw, the automatic refundable tax credits from the President's USA accounts, and the concept of Social Security not taking in more than it needs from Sen. Moynihan. I don't believe my plan is philosophically pure, yet we owe it to our children and grandchildren to find a solution to the Social Security crisis.

We have the opportunity to save Social Security and grant every working American the opportunity to build and create real wealth that can be passed on to their children and grandchildren. Let's not waste it.

Thank you, Mr. Chairman.

Chairman ARCHER. Thank you. Thank you for your presentation. Mr. Foley, would you like to inquire?

Mr. FOLEY. I, first, want to commend Mr. Sanford. Since he arrived in Congress, he has been working aggressively to talk about Social Security, and one of my concerns is people shun and shy away from this discussion, and I don't think they should. Senator Breaux was here earlier. A number of Members have not only invited conversation but much like yourself have worked aggressively on bills that can pave the way for the future of Social Security.

Your bill, though, treats the current recipients, holds them safe, correct?

Mr. SANFORD. No, not completely. It incorporates three of—in other words, it is a subset of Kolbe-Stenholm looks at in terms of current benefit reduction for people that would be retired. And, if I might, I might name those. One, it reduces early retirement bene-

fits by about 1.6 percent a year of early retirement. Now, I would argue that it doesn't really harm a person, because our accounts are set up so that you can begin withdrawing from them at age 62, and a lot of the reason that people end up taking early retirement is, frankly, because they don't have the cash. Well, if you had your personal account that had real balances in it and you could withdraw from that, it might obviate the need to take preretirement or early retirement.

Second, it reduces the 15 percent bend point, which would basically effect the top 30 percent of earners to 10 percent between 2009 and 2028, and what this amounts to, basically, is a 7-percent reduction for the top 10 percent of earners. We have tried—you know, in picking—again, because transition cost is a problem—in picking things, we tried to, frankly, focus on the folks that would benefit the most through a personal account.

And then, three, the third thing we do is the same as what Kolbe-Stenholm does and that it speeds the move from age 66 to age 67 for retirement age. Basically, there is an 11-year gap, as you might know, and it moves it up, again, from 2016 to 2027. Basically, it moves it forward.

It does those three things, which are real benefit cuts in projected Social Security benefit. Now, I would stress the word "projected," because, as we both know, Social Security, as it is presently configured is about 2 percent short based on the percentage of payroll in its ability to meet those future obligations. So, you can argue both sides of the coin. You can say, "Well, it is a cut relative to what Social Security might 1 day offer," and I would argue, "Well, it is not really cut, because Social Security, at least as the numbers point, won't yield off of those benefits."

Mr. FOLEY. Do you still hold a cap on the total earnings that can be assessed for Social Security purposes.

Mr. SANFORD. Yes.

Mr. FOLEY. Currently 65 I think is the amount.

Mr. SANFORD. That remains that by law.

Mr. FOLEY. You don't do anything to change any of the structures?

Mr. SANFORD. It is a little higher than 70 and change, but it leaves what is in by law in place. It does nothing to change that.

Mr. FOLEY. And it doesn't do anything to expand other than what is currently prescribed by the law, the retirement age going to 67 by the year 2000?

Mr. SANFORD. Correct. Again, it speeds it, though, but——

Mr. FOLEY. Right.

Mr. SANFORD [continuing]. But, yes.

Mr. FOLEY. And what would be the impact, though, for a young person? I guess, the best way to view your formula is the longer a person has to go into the personal accounts, the more likely they will buildup a retirement nest egg. Is there a nexus point between when they really become very, if you will, rewarded for this new type of vehicle?

Mr. SANFORD. We have not been able to get the final numbers back on what the break-even point is. I am certain there would be a break-even point. But, again, because we have just sort of put this bill together, and I guess what we are looking at is the biggest

benefit to a young person would be, is a bird in the hand worth two in the bush? Most of the young people I talk to say, "Absolutely, yes" when it comes to Social Security dollars. While they may not be completely certain of what Social Security can or cannot deliver down the road, what they would be certain of would be x number of dollars sits in my personal Social Security account, and I know that it is there.

So, certainty would be one of the primary benefits, and then, again, the way we have constructed it is that it is very progressive. The lower you are on the income scale, the more you would basically get. I mean, for instance, the bottom 20 percent of the work force would not have a carve-out. In other words, they would get whatever they put into their personal account and the full value of whatever is promised based on current law with Social Security, and we would graduate up from there. So, we have tried to design it progressively, and the biggest thing, though, that I would say that a young person would get would be certainty.

Mr. FOLEY. Thank you.

Mr. HOUGHTON [presiding]. OK, well, any other questions? Well, thanks very much, Mark. We appreciate you——

Mr. SANFORD. I thank you, sir.

Mr. HOUGHTON. OK, great.

Mr. Smith.

STATEMENT OF HON. NICK SMITH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Mr. SMITH of Michigan. Mr. Chairman, thank you very much. I would like to give everybody who is left some caffeine. You have tremendous endurance listening to 7 hours of Social Security proposals today. So my compliments to the Committee to consider one more.

When I first came to Congress in 1993, I introduced my first Social Security bill. In fact, I wrote it while I was chairing the Senate Tax Committee in Michigan. In the following session, in the 104th, I introduced a bill that was scored by the Social Security Administration to keep Social Security solvent. Likewise, I introduced another scored bill last session and every time, I would like to think, there have been some improvements.

What I would like to do is just go through what my guidelines were for how to structure a Social Security bill and I have called them the "Ten Commandments for Social Security Reform." The first commandment that I decided is time is our enemy and we must move without delay. The bill that I introduced in 1994 was much less drastic than is required now because of the time lag and because we have waited.

The second commandment that I have used to guide my bill is we need to take into account the growing probability of the significant rise in life expectancy. So what is used by the actuaries now is probably underestimating the length of time that individuals are going to live after they reach retirement age. Both Ken Manton and William Haseltine appeared before my Budget Committee Task Force on Social Security. I chair the Task Force, a bipartisan Task Force, that has been holding meetings every Tuesday to bring in witnesses in this regard.

Third, we must move quickly and boldly but the change itself must be gradual.

Fourth commandment is the burden of adjustment must fall equitably. Any change should hold current retirees harmless and they should receive full cost of living increases. And those near their retirement years and low-income workers should be protected. In other words, there has to be a safety net.

The fifth commandment is no tax increases. If I am not mistaken, my bill may be the only one that would not require a tax increase, either a FICA tax increase or a general tax increase for those proposals that use General Fund to accommodate some of the transition costs.

The sixth commandment is every worker should enjoy the benefits of savings and investment.

Seven is investments made for retirements must be prudent.

The eighth is money managers should not earn excessive fees. In our estimates on the fees, the administration charges are two basis points. So we are estimating for what we call a first-tier investment and a second-tier investment that gives the individual owner of those PRSAs some latitude. It would amount to two basis points or two one-hundredths of a percent for the cost of administering.

The ninth commandment compels us to redesign Social Security so that it commands full public confidence.

The tenth commandment is to maintain our lead in a competitive global economy. How do we have this transition? How do we make sure that we are not going to go in the direction of Finland and Germany? Germany right now charges 50 percent of a worker's earnings to accommodate their retiree program. Let us not get in that predicament. You can't read that from there, can you?

Mr. SHAW [presiding]. Nick, we are having a problem with the sound.

Mr. SMITH of Michigan. The workers own and invest a portion of their Social Security taxes by creating a personal retirement savings account and are limited to——

Mr. SHAW. I will tell the gentleman that even though this is a powerful Ways and Means Committee, you do not have to kneel. [Laughter.]

Mr. SMITH of Michigan. You can't fool me. I start at 2.6 percent of payroll for the Personal Retirement Savings Accounts, or PRSAs. I use the General Fund surpluses for 8 years coming out of the General Fund not to exceed the surplus coming into Social Security to help make the transition.

I limit the investments to index stocks, index bonds, index small cap funds, and index global funds. In other words, roughly the same as the Thrift Savings Plan options now. But in addition, we allow the Secretary of the Treasury to allow additional safe investments.

I use the surpluses coming into the Social Security Trust Fund to finance the PRSAs. There is no increase in taxes or government borrowing. Adding a bend point gradually slows down the growth of benefits, by a small amount each year, for high-income retirees. Now this is how we pay for it to a large extent. Because the initial 2.6 percent private investment that eventually gets to 8.4 percent, out of the 12.4 percent Social Security tax, we add an additional

bend point or, in effect, we slow down the increase in benefits for the high-income retiree. It saves money and helps allow for the transition costs, putting more money into PRSAs. And it is reasonable and logical because the 2.6 percent of $74,000, which is the current taxable income, gives that individual a lot more opportunity in savings and accruing the magic of compound interest than a $20,000 or $30,000 individual. To compensate for that advantage, we make the fixed benefit part of Social Security more progressive.

And the next blip down is on how we divide PRSA contributions. For women, there is a couple of things that we do. One, is divide the contributions so we take the eligible investment money that a husband has and that the wife has, we add them together so each spouse is allowed identical amounts of money that they can invest in their own PRSA. It sort of gyps some of the attorneys maybe later on if something happens to that marriage, but as long as they are married, both of them would have the opportunity to invest the exact same amount.

The widows and widowers benefits are increased from 100 percent to 110 percent. As we have talked to a lot of widows and surviving spouses, the cost at 100 percent of maintaining that house has forced a lot of these individuals into nursing homes so we up that, at a small cost, to 110 percent, hopefully to keep them in their homes instead of going into nursing homes. And then we maintain a trust fund reserve so that there is always at least a half a year in the trust fund reserve.

Excuse this presentation, and I'll be glad to react to any questions.

[The prepared statement and attachments follows:]

Statement of Hon. Nick Smith, a Representative in Congress from the State of Michigan

Chairman Archer and Ranking Democrat Rangel, thank you for organizing today's hearing. If we want to be able to keep the promises the government is making to future retirees, we must enact reforms now that restore solvency to this vital program

As a member of the 104th Congress, I introduced the first reform plan in the House this decade that provided private retirements savings accounts and was scored to keep Social Security solvent. That bill, "The Social Security Solvency Act of 1996," was updated and re-introduced as "The Social Security Solvency Act of 1997." Shortly, I will introduce "The Social Security Solvency Act of 1999."

As you may know, I was appointed Chairman of the Budget Committee Task Force on Social Security in January. The Task Force has met weekly since March, receiving statements from national experts including Alan Greenspan, Larry Summers, and actuaries from the Social Security Administration. We have also heard from top demographers, investment experts, and mutual fund administrators. Yesterday, the AARP appeared before us. We anticipate finishing our fact finding at the end of this month and will distribute a report to all Members.

Today, I would like to present a summary of what the Task Force has learned and argue in favor of my "Social Security Solvency Act of 1999," which I will introduce shortly. Although there are some important refinements, this Act is patterned on the "Social Security Solvency Act of 1997" that I introduced previously. Like the 1997 bill, it has been scored by the actuaries as restoring the solvency of America's most popular public program. The development of my plan follows from what I consider to be the Ten Commandments of Social Security reform.

THE TEN COMMANDMENTS FOR SOCIAL SECURITY REFORMERS

The first commandment is that TIME IS OUR ENEMY AND WE MUST MOVE WITHOUT DELAY. Alan Greenspan informed us in March that OASDI has an unfunded open liability of $9 trillion 1999 dollars. This means that an outside party

would require an up-front payment of $9 trillion now, plus the legal right to 12.4% of 85% of the nation's payroll forever just to honor the promises we have made to present and future retirees, survivors, and disabled individuals. This obligation is very real, and it exceeds by almost three times the size of the national debt held by the public. Every year we delay, this unfunded liability goes up by hundreds of billions of dollars as we grow closer to the day when Social Security's temporary positive cash flow first halts, then stops forever.

Put another way, to keep Social Security solvent for just the next 75 years, it would take an across-the-board cut in Social Security benefits of 14% for current or all future beneficiaries to make up the shortfall if we act now. Alternatively, a 16% increase in Social Security taxes would also eliminate the shortfall. These representative figures will get larger the longer we delay.

In 1983, the Congress felt an urgent need to act when Social Security had an unfunded liability of −1.82% of taxable payroll. The system now has an unfunded liability of −2.07%, a problem that is 15% larger than the one in 1983! With the danger so high, we must act with at least the same sense of urgency. Anyone who says we have the luxury of time to tackle this difficult subject is committing the nation to wrenching changes later rather than less dramatic corrections now.

The second commandment is that WE MUST REFORM THE SYSTEM TO TAKE INTO ACCOUNT THE GROWING PROBABILITY OF A SIGNIFICANT RISE IN LIFE EXPECTANCY. Dramatic increases in life spans is wonderful news. Dr. Kenneth Manton, one of America's most respected demographers, told the Task Force to expect to see many of our next generation celebrating their 100th birthday. Dr. William Haseltine, a recognized expert on aging and regenerative biology and President of a company that expects to complete mapping the human genome in the next few years, thinks that science will make even greater advances. He believes that many of our children will live to 120. As life expectancy increases, we must create opportunities for our elderly population to remain productive and active long into that period of life we now call "retirement."

Third, WE SHOULD MOVE PRUDENTLY BUT BOLDLY. Our actions must equal the scope of the problem before us. Fortunately, it is now possible to solve our problems by making gradual and continual Solvency. It took 60 years to create the current crisis. We can resolve it in steady measured steps over 50 years.

The fourth commandment is that THE BURDEN OF ADJUSTMENT MUST FALL EQUITABLY. Any change should hold current retirees harmless. They should receive full cost-of-living increases. Those near their retirement years and low income workers should also be protected. Meanwhile, better paid workers should contribute more than those with moderate incomes.

The fifth commandment states that NO TAX INCREASES should be adopted to eliminate Social Security's unfunded liability. Medicare has very difficult problems, and added revenue will be needed to resolve them. Its unfunded liability is twice that of Social Security. Social Security reformers who use new tax revenue to solve their problems complicate efforts to resolve Medicare's difficulties—where lives, not dollars, are at stake.

The sixth commandment holds that EVERY WORKER SHOULD ENJOY THE BENEFITS OF SAVING AND INVESTING. A primary reason why the rich are outpacing the lower and middle classes is their ability to invest in thriving corporations that yield returns that significantly exceed those received by putting funds in banks. Professor Roger Ibbotson, the nation's foremost historian on stock and fixed income markets, predicted in 1974 that the Dow would rise from 1,000 to 10,000 by the year 2000. He now projects that the Dow will reach 100,000 before 2025. A way must be found so that everyone can get a share of this $140 trillion in new wealth that will be created.

The seventh commandment dictates that INVESTMENTS MADE FOR RETIRMENT MUST BE PRUDENT. Prudent risk-taking does not require that every investment turn out brilliantly. It does require that no matter what happens every retiree have adequate funds from Social Security to remain above the poverty level.

The eighth commandment declares that professional MONEY MANAGERS SHOULD NOT EARN EXCESSIVE FEES from carrying out an essential national mission. The Task Force heard from William Shipman, a Principal of State Street Global Research, who presented the firm's detailed administrative cost model. Workers can have access to broadly diversified stock and bonds portfolios for only pennies a day. The GAO is confirming these findings, and will publish its report before the end of the month.

The ninth commandment compels us to REDESIGN SOCIAL SECURITY SO THAT IT COMMANDS FULL PUBLIC CONFIDENCE. Currently, many workers have so little faith in the System that they view their payroll taxes, not a contribu-

tions for their own retirement but, as sacrifices. While they support helping seniors, they don't personally expect to receive checks when they become seniors themselves. Social Security will never be free from political peril until all workers view participation as a valuable fringe benefit from going to work.

The tenth commandment requires us to MAINTAIN OUR LEAD IN A COMPETITIVE GLOBAL ECONOMY. Other nations are modernizing their national retirement systems. If we fail to improve ours, it will hurt our national economic performance and our standing in the world. Countries that have prepared themselves for the coming demographic changes will have strong economies that vault them ahead of their global competitors. I want the U.S. to be among that group of world economy leaders.

If you agree with these principles, you will like my plan. It is derived from them.

The Most Essential Step: Creating Personal Retirement Savings Accounts (PRSAs)

The central element of my plan is to provide all workers with Personal Retirement Savings Accounts (PRSAs) that they own and are professionally invested solely for their benefit. For the next 36 years all workers will contribute 2.6% of their pay, up to the maximum Social Security wage base, into their accounts. Individuals will choose where to invest these funds but will be offered attractive low cost, high reward, equity and fixed income index funds as well as more specialized programs if they so choose. After 2036, the actuaries say the contribution rate can rapidly climb, reaching 11% by 2074.

Here are some examples of PRSAs in action. A 20-year old worker earning $20,000 will deposit $520 the first year. Assuming a 2.5% inflation rate and she earns a pay raise 3.5% annually, the annual contributions will grow over time reaching $3,944 forty-five years from now. Over 45 years, she will place a total of $62,800 in her account. Assuming her funds were placed in an equity index fund that earned a 6.5% real rate of return, this $62,800 will grow to $422,000—4.6 times her final salary. By converting this sum into an annuity, she can expect to receive $34,500 a year for 19 years after her retirement. I choose that time period because it is how long the actuaries assume in their Social Security projections.

The amount that better-off workers will have in their accounts is proportionate. A teacher starting at $30,000 will see her account grow to $633,000, and her annual benefits for 19 years will be $51,750. A young attorney graduating from a fine law school who lands a job at $60,000 will retire a millionaire, having $1,266,000 in her account, and see annual benefits of $103,500 for 19 years.

Here are representative figures for 40 year old workers. A worker earning $20,000 today will have $59,200 in her PRSA account at 65. A $30,000 per year bus driver will have $88,800. The 40 year middle management executive will hold $177,600. These workers will see their annual retirement incomes supplemented by $5,000, $7,500, and $15,000 when the PSRAs are converted into annuities good until the anticipated time of death.

Finally, here are figures for 55 year old workers. The grocery clerk earning $20,000 now will acquire a $9,000 PRSA in ten years. The bank teller earing $30,000 now will have $15,600 while the successful architect earning $60,000 now will have $27,000 in 2010.

The point of these examples is that PRSAs grow very rapidly under the magic of compound interest. The biggest beneficiaries of PSRAs are the young and future generations. It makes sense, therefore, to take this into account when allocating costs across generations for restoring the System.

Investment Risk Can Be Managed

Fears about sudden stock market tumbles are overblown. It will be 20 years or more before the amounts at risk represent significant sums as a percentage of the resources needed to ensure a secure retirement. Put another way, even with a 2.6% "carve out" of Social Security payroll taxes, it will be far into the future before the monthly private retirement check exceeds the check received from Social Security. We will have time to evaluate investment returns and account for unexpected events that jeopardize workers retirement security long before they could happen. These fears should not prevent us from instituting needed reforms today.

I am exploring ways to reassure workers who may not have had experience with 401(k) plans or mutual funds. Although the number of happy investors has reached an all time high along with the DOW, the process may seem frightening to those who haven't personally benefitted from the Reagan-Bush-Clinton bull market. One idea that I would encourage the Committee to explore is a formal guarantee that anyone 45 or under will be guaranteed a retirement income equal to current law

benefits provided they invest their PSRAs in equity investments. We know from 200 years of stock market history that equity returns over long periods outperform all other prudent investments. Consequently, the government can offer guarantees to long term investors with confidence that there is at least a 200 to 1 chance it will never be called upon to honor them. I haven't had this provision scored by the actuaries. Therefore, I cannot present it to you in a formal way.

There are other ways cautious investors can avoid risk. First, they can transfer the risk of market downturns to others who accept it voluntarily. There are many life insurance and annuity products that do just that. Insurance companies are professional risk takers, and are quite successful at it. Many annuity investors give up the chance for large gains, but they avoid losses in exchange. Here's another example. Right now, a large investment house offers the public for a fee a bundle of equities with the right to sell it back to them at the price you paid for it five years from now. As Will Rogers once said, "Sometime the important thing isn't the return on capital. It's the return of capital."

Paying For It

An important issue that any reformer must confront is how to finance the transition to a modern system. We start deep in the hole with a $9 trillion unfunded liability. The problem becomes harder when 2.6% or more of taxable payroll is channeled into PRSAs, and widows benefits expanded by 10% as I propose.

Fortunately, the problem can be resolved under a policy of "easy does it" and "steady as she goes." My answer is to slow down the growth of benefits by a small amount each year for a long time. Under currently law, OASDI benefits will increase by 90%, after inflation, over the next 75 years. If we agree that real benefits should grow at a slower rate, then we can solve this problem.

My bill does this by amending the benefit formula. Before presenting my amendments, I wish to first review how initial Social Security benefit checks are determined. Under current law, a worker at normal retirement age earns a monthly benefit check known as the "primary insurance amount" or PIA. The PIA is calculated in steps. First, a worker's entire earnings record, from teenage years to retirement, is updated for inflation. Then, only the highest earning 35 years are isolated. Next, these best earning years are averaged to get an average annual earnings level. Finally, this total is divided by 12 to get "Average Indexed Monthly Earnings" or AIME.

Social Security is often described as a progressive program. The reason for this belief is that the PIA is derived from AIME in a progressive way. In 1999, anyone with an AIME of $505 or less, the equivalent of only $6,060 in year, will receive 90% of this amount annually. Anyone with an AIME of $3,043 will receive 90% of the first $505 of AIME, then 32% of the remaining amount. Anyone with an AIME in excess of $3,043 will receive 90% of the first $505 of AIME, 32% of the next $2,538, and only 15% of any remaining amounts. As you can see, Social Security provides 90% of the earnings of a very low paid worker's historic pay while only 42% of workers who averaged earnings of $36,000. The wage replacement percentage dips lower for the best off participants. The 1999 dollar thresholds of $505 and $3,043 where the benefit rates shift are known as "bend points." Under current law, they are annually increased by changes in average nominal wages.

I propose to make the Social Security system more progressive by slowing down the growth rate of benefits for those in the 32% and 15% benefit brackets. I do this first by phasing in a 5% bracket over five years that only the highest paid workers would face. It would start at AIME above $3,720 if fully in effect today. Next, I propose that the 5% and 15% brackets gradually decline at a 2.5% rate. In the first adjustment year for example, they would be 4.875 (5 x 0.975) and 31.2% (32 x 0.975). Five years out they would be 4.41 (5 x 0.985 x 0.985 x 0.985 x 0.985 x 0.985) and 28.2% (32 x 0.985 x 0.985 x 0.985 x 0.985 x 0.985). I propose that the 32% rate also decline but by only 2% a year, not 2.5%. I want the lowest paid workers to be unaffected or unambiguously better off from my changes. Consequently, the 90% rate is not subject to reduction.

As a further way to slow down the growth rate in real benefits, I proposed that the 15% and 5% bend points, and their future derivative rates, be indexed to changes in the CPI, not nominal wages. The bend point that defines the 90% AIME credit level will continue to rise with nominal wages.

I believe the mechanism under my bill, which generates a very gradual change annual change over a long period of time is a fair way to allocate the costs across generations and income levels. It's true that high school kids and young workers today would make the largest contributions to solvency. However, as we saw earlier, they have the time to benefit from the magic of compound interest. The two pay-

ment streams, one from Social Security, the other from PRSAs, together will exceed the amount of benefits projected under current law just from Social Security.

It's worth remarking that our youngest workers have the least faith that they will ever receive a Social Security benefit. In one famous poll, a larger number said they believed in UFOs than they would collect Social Security. Young workers will especially like having a binding property right in their own privately managed PRSA while giving up only some of a Social Security benefit many never expect to see in the first place.

Gradually Raising the Retirement Age As Life Expectancy at Age 65 Rapidly Improves

There are two other reforms required to restore Social Security to long-term health. The first requires thinking through a pleasant subject, increasing life expectancy during our retirement years. The actuaries predict that newborn children today who reach 65 years of age will live 3 years longer than those who reach that age now. The difference in life expectancy works out to about ½ additional month of life for every passing year. This means an infant born today who reaches his 65th birthday can expect to live until 85.5, compared to 82.5 today.

I propose that we all share our good fortune of living longer with the taxpayers. After all, we'll have more time to prepare for it! I propose eliminating the 11 year hiatus in current law between 2005–16 where the retirement age remains at 66 before increasing in 2 month increments in 2017 to 2021. Instead, I recommend raising it to 67 by 2010, then indexing it to life expectancy. The indexing provision may be the most important idea in the bill if the Task Force experts prove prescient and our children and grandchildren are destined to led much longer lives than we. Reflecting on the age of this Committee's venerable Chairman and my upcoming 65th birthday, I think the vast majority of future workers, who can be expected to be in better shape than we are today, are up to the task. For those who are not, we should update the disability program. For those who want to retire early, we should let them do so, as is now done, with actuarially fair reduced benefits.

Sharing the PRSA Bounty With the Taxpayers

The final reform shares certain features with the reform plan proposed by Chairman Archer and Subcommittee Chairman Shaw, Jr. As the size of PRSAs grows, the need for taxpayer assistance declines. We can ask for an especially large contribution from that young attorney who will have a PRSA worth over $1,000,000 for example. I propose that PRSA accounts be offset by the future value of contributions made into PRSA assuming a 3.7% real rate of return. In effect, a worker who gets a 6.5% real rate of return from equity investments will keep 2.8%. The remaining 3.7% is returned to the Trust Funds so they balance. A 2.8% real rate of return is much higher than the 1% or less experts now predict on future OASDI payroll tax payments if, and it's a big if, Congress finds a way to honor all benefit promises under current law. I wish it could be higher. But as Billy Joel sang, "We didn't start the fire. It's been burning since the world been turning." We have to eliminate the $9 trillion shortfall we've been handed or leave a more difficult challenge to future leaders who will lead if we refuse the challenge.

Actuarial Scoring of the Social Security Solvency Act

Here is the summary table the Social Security actuaries.

Estimated Long-Range OASDI Financial Effect of Proposal of Representative Nick Smith

Section		Estimated Change in Long-Range OASDI Actuarial Balance [1]
201	Raise the NRA by 2 months per year for those age 62 in 2000 to 2011, then index to maintain a constant ratio of expected retirement years to potential work years.	0.50
202	Provide a third PIA bend point in 2000 with a 5% percent factor; index the second and third bend points by the CPI and gradually phase down the 32, 15 and 5 percent factors after 2000.	2.89
203	Annual statement for workers and beneficiaries	(2)

Estimated Long-Range OASDI Financial Effect of Proposal of Representative Nick Smith—Continued

Section		Estimated Change in Long-Range OASDI Actuarial Balance[1]
205	Cover under OASDI all State and local government employees hired after 2000.	0.21
206	Increase benefit payable to all surviving spouses by 10 percent beginning 2001.	–0.30
207	SSA study the feasibility of optional participation	[2]
....	Subtotal for sections 201, 202, 203, 205, 206, 207	3.21
101	Set up PRSA accounts starting 2001	....
102	Redirect 2.6 percentage points of OASDI payroll tax to PRSAs for 2001–2036. After 2036, redirect to PRSAs any OASDI income in excess of the amount needed to cover annual program costs and maintain a minimal contingency reserve trust fund. Transfer specified amounts from the Treasury to OASDI for years 2001–9 (based on current CBO surplus est).	....
103	Reduce OASI benefit levels by the smount of lifetime PRSA contributions, accumulated at the yield on trust fund assets plus 0.7 percent.	– 1.15
....	Total for proposal	2.06

[1] Estimates for individual provisions exclude interaction
[2] Negligible, i.e., less than 0.005 percent of payroll
Based on the intermediate assumptions of the 1999 Annual Trustees Report Office of the Chief Actuary Social Security Administration June 5, 1999

The Impact of the Plan on the Unified Budget

The Social Security Solvency Act has a very salutary effect on the long run unified budget. Under current law, the nation will experience a dramatic swing in the unified budget over the next sixty years. Until most of the baby boomers retire around 2020, the nation can expect to run unified budget surpluses. For the fifty years or longer that follow 2020, the unified budget will plunge into the red with accelerating speed. My bill helps to stabilize the unified budget over the long run by reducing the size of surpluses now and reducing the size of the deficits that appear after 2020. The bill principally reduces unified surpluses now by channeling a portion of payroll receipts into PSRAs. By amending the benefits formula, it reduces unified budget deficits significantly later on. Overall, my bill makes the government smaller. Both taxes and spending as a share of GDP fall significantly in the middle of the next century.

My bill's primary impact in the early years is to reduce revenues by 2.6% of taxable payroll, starting in 2001. Table II F7 of the Social Security 1999 Trustees Report specifies how much revenue, by year, 12.4% of taxable payroll tax raises for the several years. By calculating what fraction 2.6 is of 12.4, then multiplying by projected taxable payroll receipts its possible to calculate how much the bill reduces revenues. We estimate these revenue reductions will be offset by $12 billion annually by 2008 by bringing newly hired state and local government workers under Social Security.

My bill also provides for a 10% increase in widows/widower benefits. Short term outlays also will increase because less federal debt will be retired due to the revenue reductions and outlays increases, resulting in higher interest expenses.

Gradual reduction in benefits, due to indexing the bend points to the CPI rather than nominal wages, and gradual phasing down the 32%, 15%, and 5% benefit factors, will reduce outlays by growing amounts. Benefits are further reduced through the 3.7% offset formula described above.

The combined impact of all these changes is shown in the following table:

Impact of the Major Provisions of the Social Security Solvency Act on the Unified Budget

($Bil)

Year	Debt	Widow/Widower	Benefits	Total Outlays	Revenues	Impact on Unified Budget
2001	+5	+9	−1	+13	−95	−108
2002	+9	+9	−3	+15	−97	−112
2003	+14	+9	−4	+19	−100	−119
2004	+19	+9	−6	+22	−104	−126
2005	+24	+10	−9	+25	−109	−134
2006	+29	+10	−14	+25	−113	−138
2007	+34	+10	−19	+25	−117	−142
2008	+39	+10	−25	+24	−122	−146
	....	....	Totals:	+205	−857	−$1,025

To comply with reconciliation instructions, the Committee could elect to defer some contributions into PRSA accounts from 2001–4 until 2005–8. Additional revenue would have to be found since estimated revenue losses total $857 billion from 2000 to 2008 while the instruction limits reductions to $778 billion from 2000 to 2009. Spending offsets will be needed to pay for the widow's benefit.

THE ACT PREVENTS DANGEROUS FUTURE UNIFIED BUDGET DEFICITS

Percent of Taxable Payroll

Year	Current Law Income Rate	Current Law Cost Rate	Annual Balance	Smith Bill Income Rate	Smith Bill Cost Rate	Annual Balance
2010	12.75	11.91	.84	10.13	11.3	−1.18
2020	12.91	15.03	−2.12	10.22	11.86	−1.63
2030	13.09	17.71	−4.62	10.33	11.98	−1.65
2040	13.17	18.18	−5.00	9.62	9.85	−0.23
2050	13.22	18.28	−5.06	7.1	7.26	−0.17
2060	13.29	19.05	−5.77	5.02	5.14	−0.12
2070	13.34	19.63	−6.29	3.09	3.18	−0.09

After 2015, my bill substantially reduces future unified budget deficits. The precise amounts are difficult to calculate 15, 25, or 50 years out. However, their magnitude can be suggested from the actuaries' scoring. Under current law, the 1999 Trustees Report found that OASDI would run deficits starting in 2015 by growing amounts. By 2040, OASDI will run deficits equal to 5.00% of taxable payroll and growing. Under my plan, OASDI will run only a minor deficit of 0.23% of taxable payroll, and it will be falling. Here is a comparison of the two actuarial projections. It proves that my bill avoids the creation of massive unified deficits for most of the 21st century. It therefore stabilizes long-run fiscal policy.

IMPACT ON THE SOCIAL SECURITY TRUST FUNDS

Instead of exhausting the Trust Funds in 2035, my plan keeps them in the black.

Year	Trust Fund Ratio	Year	Trust Fund Ratio	Year	Trust Fund Ratio
2005	241%	2035	54%	2065	49%
2015	267%	2045	45%	2074	68%
2025	159%	2055	45%	....	....

*The Trust Fund Ratio equals the amount of assets on hand divided by that year's disbursements

USE OF GENERAL REVENUES

I believe solving Social Security's problems is so important we should apply the proceeds from of on-budget surpluses from 2000 until 2008 to achieve it. Importantly, the plan still provides room for tax relief, improving Medicare's unstable financing, or a reduction in the national debt.

($Billions) The Smith Plan Reduces, but Does Not Eliminate, Short-term Unified Budget Surpluses

Year	2001	2002	2003	2004	2005	2006	2007	2008
Off-Budget	145	153	161	171	183	193	204	212
On Budget	6	55	48	63	72	113	130	143
Smith Plan	–107	–111	–118	–125	–132	–137	–141	–146
Remaining Surplus	+44	+98	+91	+109	+123	+169	+193	+209

Every day of delay leaves us with fewer resources to bring solvency to Social Security. Right now, the system is enjoying robust surpluses. In fifteen years, these surpluses will be gone, replaced by deficits that grow larger each year. We must act now for the baby boomers' retirement.

CONGRESSMAN NICK SMITH'S SOCIAL SECURITY SOLVENCY ACT:

** Allows workers to own and invest a portion of their Social Security taxes by creating Personal Retirement Savings Accounts (PRSAs).
** PRSA investment starts at 2.6% of wages and gradually increases.
** PRSA limited to a variety of safe investments.
** Uses surpluses coming into the Social Security Trust Fund to finance PRSAs.
** No increases in taxes or government borrowing.
** PRSA account withdrawals may begin at 59 ½, while the eligibility age for fixed benefits is indexed to life expectancy.
** Tax incentive for workers to invest an additional $2,000 each year.
** Gradually slows down benefit increases for high income retirees.
** Divides PRSA contributions between couples to protect low income and non-working spouses.
** Widows or widowers benefit increased to 110% of standard benefit payment.
** Scored by the Social Security Administration to keep Social Security solvent.
** Maintains a Trust Fund reserve.

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A. PLANS THAT ACHIEVE 75-YEAR SOLVENCY

1. **Archer/Shaw**

   The plan would provide workers with a tax credit equal to 2 percent of their Social Security taxable wages financed with general revenues. The tax cut would be automatically deposited into individual accounts. Upon retirement, account balances would be used to help finance the worker's current law benefit or higher.

2. **Kolbe/Stenholm/Dooley/McCarthy/Smith/Sanford/Greenwood**

   The plan would divert 2 percentage points of the current 12.4 percent payroll tax to individual accounts modeled after the Federal Thrift Savings Plan. Upon retirement, workers would receive a reduced benefit from Social Security plus their individual account proceeds. Some low-income workers would receive a greater benefit from Social Security relative to current law in addition to their account balances.

3. **Nadler/Pelosi/Lee/Vento**

   The plan would transfer 62 percent of projected budget surpluses to the Social Security Trust Funds over the next 15 years, as proposed by the President. An independent board would be authorized to hire private managers to invest up to 30 percent of the Trust Funds' assets in broad stock index funds. (The President's plan would allow up to 15 percent of the Trust Funds' assets to be invested privately.) In addition, the amount of wages subject to the payroll tax would be increased, thereby raising benefits accordingly.

4. **Smith (Nick)**

   The plan would divert 2.6 percentage points of the current 12.4 percent payroll tax to individual accounts. Upon retirement, account contributions grown at a hypothetical rate of return would offset a worker's Social Security benefits. In the long run, the amount of payroll taxes diverted to individual accounts would increase and account balances would mostly replace retirement and survivor benefits from Social Security. The plan would also modify the benefit formula and transfer on-budget surpluses to the Social Security Trust Funds over the next 10 years.

5. **Sanford**

   The plan would provide workers with a tax rebate funded with Social Security surpluses. The rebate would be automatically deposited into individual accounts. Upon retirement, account balances would be used to help finance the worker's Social Security benefit.

6. **Gregg/Breaux/Kerrey/Grassley/Robb/Thompson/Thomas**

The plan would divert 2 percentage points of the current 12.4 percent payroll tax to individual accounts. Upon retirement, workers would receive a reduced benefit from Social Security plus the proceeds from their individual accounts.

7. **Gramm**

The plan would divert 3 percentage points of the current 12.4 percent payroll tax to individual accounts. The Trust Funds would be reimbursed with general revenues for a transitional period. Upon retirement, account balances would be used to purchase a private annuity. The annuity would be supplemented by the Social Security system if it is less than the worker's current law benefit plus a bonus equal to 20 percent of annuity.

8. **Moynihan/Kerrey**

The plan would finance Social Security on a strict pay-as-you-go basis by reducing payroll tax rates immediately and increasing them as program costs rise. The growth in program costs would be contained through several benefit revisions.

B. How Benefits Are Calculated under Current Law

- When a worker applies for Social Security benefits, his/her 40 years of highest earnings are adjusted for wage inflation.

- The five years of lowest earnings are dropped.

- The remaining 35 years of highest earnings are added together and divided by 420 (i.e., the number of months in 35 years.) This calculation yields the worker's **Average Index Monthly Earnings (AIME).**

- The worker's basic monthly Social Security benefit equals:

    90% of the first $505 of the AIME plus
    32% of the amount between $505 and $3,044 plus
    15% of the amount over $3,044

- The dollar amounts in the benefit formula ($505; $3,043; $3,044) are called **bend points** and the percentages (90%; 32%; 15%) are called **bend point factors.** The bend points and bend point factors are designed to replace more pre-retirement income for lower-income workers than for higher-income workers.

- Workers are eligible for their full benefit at the normal retirement age of 65. A reduced benefit is paid if workers retire early (the earliest age of eligibility is 62). Workers who retire after the age of 65 receive a delayed retirement credit that increases their monthly benefit. The reduction for early retirement and the increase for delayed retirement are designed to result in the same amount of lifetime benefits at any age the worker chooses to retire.

- Under current law, the normal retirement age is scheduled to increase from 65 to 67 by the year 2027. The early retirement age will remain at 62. The increase in the normal retirement age will increase the penalty for retiring early and the reward for delaying retirement.

- Each year, the worker's monthly benefit is increased to reflect inflation. This annual cost-of-living-adjustment (COLA) is pegged to the consumer price index (CPI).

The following page provides an example of the benefit calculation for a worker who attains age 62 in 1999. The calculation assumes that the worker has always earned average wages.

Example of Benefit Calculation for Average Wage Earner Attaining Age 62 in 1999

EARNINGS HISTORY FOR WORKER WHO EARNED AVERAGE WAGES THOUGHOUT CAREER

Year	Annual Earnings	Inflation Index	Inflation-Adjusted Earnings
1959	$ 3,856	7.11	~~$ 27,426~~
1960	$ 4,007	6.84	~~$ 27,426~~
1961	$ 4,087	6.71	~~$ 27,426~~
1962	$ 4,291	6.39	~~$ 27,426~~
1963	$ 4,397	6.24	~~$ 27,426~~
1964	$ 4,576	5.99	$ 27,426
1965	$ 4,659	5.89	$ 27,426
1966	$ 4,938	5.55	$ 27,426
1967	$ 5,213	5.26	$ 27,426
1968	$ 5,572	4.92	$ 27,426
1969	$ 5,894	4.65	$ 27,426
1970	$ 6,186	4.43	$ 27,426
1971	$ 6,497	4.22	$ 27,426
1972	$ 7,134	3.84	$ 27,426
1973	$ 7,580	3.62	$ 27,426
1974	$ 8,031	3.42	$ 27,426
1975	$ 8,631	3.18	$ 27,426
1976	$ 9,226	2.97	$ 27,426
1977	$ 9,779	2.80	$ 27,426
1978	$ 10,556	2.60	$ 27,426
1979	$ 11,479	2.39	$ 27,426
1980	$ 12,513	2.19	$ 27,426
1981	$ 13,773	1.99	$ 27,426
1982	$ 14,531	1.89	$ 27,426
1983	$ 15,239	1.80	$ 27,426
1984	$ 16,135	1.70	$ 27,426
1985	$ 16,823	1.63	$ 27,426
1986	$ 17,322	1.58	$ 27,426
1987	$ 18,427	1.49	$ 27,426
1988	$ 19,334	1.42	$ 27,426
1989	$ 20,100	1.36	$ 27,426
1990	$ 21,028	1.30	$ 27,426
1991	$ 21,812	1.26	$ 27,426
1992	$ 22,935	1.20	$ 27,426
1993	$ 23,133	1.19	$ 27,426
1994	$ 23,754	1.15	$ 27,426
1995	$ 24,706	1.11	$ 27,426
1996	$ 25,914	1.06	$ 27,426
1997	$ 27,426	1.00	$ 27,426
1998*	$ 28,315	1.00	$ 28,315
		Sum of 35 highest years	$ 960,799

Benefit Calculation:

1. Past 40 years of earnings are adjusted for wage inflation

2. 5 lowest years of earnings are dropped, leaving the 35 years of highest earnings

3. 35 years of highest earnings are summed and divded by 420 to yield the worker's AIME

   $$\frac{\$960{,}799}{420} = \$\ 2{,}288$$

4. Monthly benefit equals:

90% of first $505 plus	$	455
32% of next $2,539 plus	$	570
15% of amount over $3,044	$	
Monthly benefit	**$**	**1,025**

This is the worker's primary insurance amount (PIA). The PIA is reduced if the worker retires early, and it is increased if the worker delays retirement past the normal retirement age.

*The last year of earnings is not adjusted for inflation because there is a one year lag in collecting average wage data.

C. ARCHER/SHAW

- All workers would receive an annual refundable tax credit equal to 2 percent of their Social Security taxable wages (maximum credit is $1,452 in 1999).

- The tax credit would be financed with general revenues. Over the first 15 years, the accounts would be fully funded with Social Security surpluses.

- The tax credit would be automatically deposited into each worker's Social Security Guarantee Account. Workers could choose to invest their account in one of several qualified mutual funds. Initially, all funds must be invested in a fixed mix of 60 percent stock index funds and 40 percent corporate bonds.

- Upon retirement, the Social Security Administration would calculate a monthly pay out (similar to an annuity calculation) based on the Guarantee Account balances. Workers would receive a lifetime benefit equal to the their current law benefit or the monthly account pay out, depending on which is greater.

- There are no benefit reductions. All workers are guaranteed their current law benefit. Some workers could receive benefits higher than those provided under current law if their investments outperform historical averages.

- Each month, the monthly account pay out would be transferred from the worker's Guarantee Account to the Social Security Trust Funds to help finance the worker's benefit.

- The current 12.4 percent payroll tax rate would be reduced to 9.9 percent by 2050 and to 8.9 percent by 2060.

- The earnings limit would be eliminated for all beneficiaries (age 62 and over).

- Workers who die prior to collecting Social Security benefits could leave account balances to their heirs tax free after supporting survivor benefits.

D. Kolbe/Stenholm

- All workers under the age of 55 would be required to divert 2 percentage points of their payroll tax into individual security accounts (ISAs).

- Workers could make voluntary contributions of up to $2,000 annually. Low-income workers would receive a 50 percent government match funded with general revenues.

- The administrative and investment structure of the ISAs would be modeled on the Federal Thrift Savings Plan.

- Upon retirement, workers would receive a reduced benefit from Social Security plus the proceeds of their ISAs.

- The proposals includes the following benefit adjustments:
  - COLAs would be reduced for all beneficiaries based on revisions to the CPI.
  - The already-scheduled increase in the normal retirement age from 65 to 67 would be accelerated. Thereafter, the normal and early retirement ages would be indexed for increases in life expectancy.
  - In addition, there would be an across-the-board benefit reduction to reflect the fact that people are spending more years in retirement.
  - The benefit reduction for early retirement would increase, but the benefit enhancement for delayed retirement would also increase.
  - The benefit computation period would be extended from 35 years to 40 years. The effect of this provision would be partially mitigated by including all years of earnings in the numerator of the benefit formula. This provision would not apply to disabled workers or the lower-wage earner of married couples.
- The benefit formula factors would be gradually reduced for middle- and high-income workers.

- Workers could retire at any time as long as their accounts provide a minimum benefit equal to 100 percent of the poverty level.

- A worker's total benefit may be greater than or less than their current law benefit, depending on their account balances at retirement. However, workers with at least 20 years of covered earnings would be guaranteed a minimum benefit equal to 60 percent of the poverty level in addition to their ISA balances. This amount would be phased up to 100 percent of the poverty level for workers with at least 40 years of covered earnings. The minimum guaranteed benefit would provide some low-income workers with a larger benefit than what they are entitled to under current law.

- The plan would reduce the CPI for all federal programs and provisions indexed to the CPI, including the federal income tax code. The resulting revenues and savings would be transferred to Social Security to help pay workers' benefits. The transfer would be specified in the law as a percent of taxable payroll, increasing from 0.03 percent of taxable payroll in 2000 to 0.8 percent of taxable payroll in 2060 and thereafter.

- Revenue from the taxation of Social Security benefits, which is now credited to Medicare, would be redirected to Social Security.

- The earnings limit would be eliminated for beneficiaries who work past the normal retirement age.

- At death, workers could leave their account balances to their heirs. The transfer is tax free if the balances are rolled over to another worker's account; otherwise, they are taxed as regular income.

E. Nadler

- Over the next 15 years, 62 percent of the projected budget surpluses would be transferred from the General Fund of the Treasury to the Social Security Trust Funds. The transfer would be specified in the law as a percent of taxable payroll, increasing from 2.2 percent in 2000 to 4.51 percent in 2014. These percentages would be adjusted as more complete data become available.
- Each year, 60 percent of the transfer would be held in the form of special-issue Treasury securities, and 40 percent of the transfer would be used to purchase broad stock index funds.
- All dividends would be reinvested in broad stock index funds until 30 percent of the Trust Funds' total assets are held in stock.
- The purchase of stock index funds would be directed by an independent board authorized to hire private fund managers.
- The plan would further increase Social Security's income by increasing the amount of wages subject to the payroll tax relative to current law. Future benefits would increase accordingly for affected workers.
- There would be no benefit reductions.

F. Smith

- All workers under the age of 65 on January 1, 2001 would be required to divert 2.6 percentage points of their payroll tax into Personal Retirement Savings Accounts (PRSAs). After 2036, the portion of the payroll tax diverted to individual accounts would be determined based on the financial status of the Social Security Trust Funds.
- Initially, workers could choose among three index funds invested in a fixed mix of stocks and bonds. Once the accounts grow to a certain level, more investment options would be available.
- For years 2001 through 2009, general revenues would be transferred from the General Fund of the Treasury to the Social Security Trust Funds. The annual transfers would grow from $11 billion in 2001 to $165 billion in 2009. These amounts reflect the on-budget surplus as estimated by the Congressional Budget Office.
- Upon retirement, a worker's Social Security benefit would be reduced by the amount of the worker's PRSA contributions grown at a specified rate. This hypothetical growth rate would equal the return on long-term bonds held by the Trust Funds plus 0.7 percentage points. Benefits for disabled workers would not be reduced until the disabled worker reached retirement age.
- By the year 2073, it is expected that retirement and survivor benefits paid by Social Security would be eliminated because the amount of the benefit reduction (based on PRSA contributions and the hypothetical growth rate) would exceed expected benefit payments under current law.
- Program costs would be further reduced through several benefit adjustments.
    - The already-scheduled increase in the normal retirement age from 65 to 67 would be accelerated. Thereafter, the normal retirement age would be indexed for increases in life expectancy.
    - A third bend point would be added to the benefit formula with an associated bend point factor of 5 percent (i.e., the bend point factors would be 90, 32, 15, and 5). The bend points and bend point factors for middle- and high-income workers would be gradually reduced.
- All workers and beneficiaries over the age of 18 would receive an annual statement indicating their total payroll tax contributions with interest and the total amount of benefits received to date with interest.
- Newly hired State and local workers would be included in the Social Security program, thus imposing a payroll tax on their wages. Full-time students would be exempt from this provision.
- Survivor benefits would be increased by 10 percent for all qualifying widow(er)s receiving benefits in 2001 and later.
- The earnings limit is eliminated. (This provision is not included in the actuaries' memo.)

G. Sanford

- All workers would receive an annual refundable tax rebate financed with Social Security surpluses. (Social Security would run annual surpluses – including interest income – for the next 75 years under this plan.) The amount of the rebate depends on the amount of the Social Security surplus in that year.

- The rebate would be automatically deposited into each worker's personal retirement account (PRA). PRAs could be set up as sister accounts to employer pension plans.

- For the first two years an account is established, low-wage workers would receive an additional $300 tax credit financed with general revenues. Tax credits financed with general revenues would also be used to pay the administrative fees of low-income workers.

- Workers can make voluntarily after-tax contributions of up to $10,000. Available documents do not specify whether this is an annual or lifetime cap.

- As with 401(k) plans, each PRA would have a limited number of investment options selected by a plan administrator. Each plan would be required to offer at least three investment options. After enrolling with a particular plan, workers can choose how to allocate assets among the investment options offered by that plan, but they cannot switch to a different plan.

- Upon retirement, workers could purchase an annuity or withdraw account balances at their discretion.

- The worker's Social Security benefit would be reduced by the amount of rebates deposited into their PRAs grown at the rate of return earned by the Trust Funds. In essence, account balances help finance the worker's current law benefit. Additional investment earnings would not reduce the worker's Social Security benefit.

- This benefit reduction would not apply to low-wage workers who would receive their current law benefit plus the proceeds of their PRAs.

- Several adjustments to Social Security benefits would be made.
  - The already-scheduled increase in the normal retirement age from 65 to 67 would be accelerated.
  - The 15 percent bend point factor affecting high-income workers would be gradually reduced to 10 percent.
  - The penalty for early retirement would be gradually increased. However, workers could access their PRAs at the age of 62 without penalty.

- None of the provisions would apply to disability benefits. The Disability Insurance program would not be affected by this plan in any way.

- At retirement, the higher earner of a married couple would be required to purchase life insurance policy that provides a survivor benefit equal to the current law benefit.

- The earnings limit for seniors who work past the normal retirement age would be eliminated

- Account balances could be left to heirs tax free.

H. Gregg/Breaux

- Beginning in 2000, all workers covered by Social Security would be required to divert 2 percentage points of their payroll tax into individual accounts.

- Workers could make voluntary contributions of up to $2,000 annually. Low-income workers would receive a government subsidy funded with general revenues.

- Workers would have an unspecified choice of investment options.

- Upon retirement, workers would receive a reduced benefit from Social Security plus the proceeds of their individual accounts. The benefit reduction would be based on the accumulation of payroll tax contributions to the accounts grown at the rate of return earned by the Trust Funds.

- The proposal includes the following benefit adjustments:
    - COLAs would be reduced for new retirees as a result of revisions to the CPI.
    - The benefit formula factors (currently 90, 32 and 15) would be changed to 90, 70, 20, and 10. This revenue-neutral change would increase the progressivity of the guaranteed benefit, presumably to compensate low-income workers who could retire with smaller account balances.
    - The already-scheduled increase in the normal retirement age from 65 to 67 would be accelerated. Thereafter, all of the bend point factors would be adjusted to account for increases in life expectancy. This adjustment would not apply to disabled workers.
    - The benefit reduction for early retirement would be increased, but the benefit enhancement for delayed retirement would also increase.
    - The benefit computation period would be extended from 35 years to 40 years. The effect would be partially mitigated by including all years of earnings in the numerator of the benefit formula. This provision would not apply to the lower-wage earner of a married couple. This provision would not apply to disabled workers.

- A worker's total benefit may be greater than or less than their current law benefit, depending on their account balances at retirement. There is no guaranteed minimum benefit.

- Over time, some surviving spouses would be given the option of receiving a survivor benefit equal to 75 percent of the couple's combined benefit when both spouses were alive.

- Social Security's annual income would be enhanced by increasing the amount of wages subject to the payroll tax relative to current law. Future benefits would increase accordingly for affected workers.

- The CPI would be reduced for all federal programs and provisions indexed to the CPI, including the federal income tax code. The resulting revenues and savings would be transferred to Social Security to help pay workers' benefits. The annual transfers would be specified in the law as a percent of taxable payroll, increasing from 0.6 percent of taxable payroll in 2000 to 1.2 percent of taxable payroll in 2060 and thereafter.

- Revenue from the taxation of Social Security benefits, which is currently credited to Medicare, would be diverted from Medicare to the Social Security Trust Funds.

- KidSave Accounts would be established for children born in 2000 and later. The accounts would be funded with general revenues. Fifty percent of accumulated balances would be used to offset the child's future Social Security benefits.

- The earnings limit would be eliminated for all beneficiaries (age 62 and over).

- At death, workers could leave remaining account balances to their heirs.

I. Gramm

- All workers entering the work force in 2000 or later would be required to divert 3 percentage points of their current payroll tax into individual SAFE accounts. Workers between the ages of 35 and 55 in 2000 would receive an additional deposit equal to 2 percent of taxable pay.
- The General Fund of the Treasury would reimburse the Social Security Trust Funds for the amount of the contributions. This reimbursement would be reduced as much as possible based on the financial status of the Social Security Trust Funds. The reimbursements would end by 2040.
- Workers could choose to invest their accounts in one of several approved funds. For the first two years, all funds must be invested in a fixed 60/40 portfolio mix of stocks and corporate bonds.
- Upon retirement, workers would use their SAFE account balances to purchase a private market annuity.
- Social Security would supplement the annuity if it does not produce a monthly lifetime benefit equal to the worker's current law benefit plus 20 percent of the annuity amount.
- There would be no benefit reductions. All workers would be guaranteed a benefit equal to their current law benefits plus a bonus equal to 20 percent of the annuity amount (the maximum bonus would be 20 percent of the worker's current law benefit).
- Workers may retire as soon as their annuity provides a benefit equal to 120 percent of their current law benefit.
- A trigger in the legislation would increase the amount of the payroll tax diverted to SAFE accounts based on the financial status of the Social Security Trust Funds.
- Based on Social Security's financial status, the payroll tax rate could be reduced from 12.4 percent to 8 percent plus the amount needed to finance disability insurance.
- The plan would "recapture" higher revenues from corporate income taxes in an effort to make SAFE Account investments tax free. Increased individual income taxes, taxation of annuities, and other revenues generated by the plan would be directed to the Social Security Trust Funds. The plan specifies the assumptions that would be used in calculating the amount of revenue generated by the plan for the first two years.
- Workers who die prior to collecting Social Security benefits could leave their account balances to their heirs tax free after supporting survivor benefits.

J. MOYNIHAN/KERREY

- Workers and employers would each receive a payroll tax cut equal to 1 percentage point. Thus, the total payroll tax rate would fall from 12.4 percent to 10.4 percent.

- Workers may voluntarily contribute the tax cut to a voluntary investment account. Employers would be required to match the contribution.

- A savings plan similar to the Federal Thrift Savings Plan would be established. Workers could invest their funds with the government plan or with the private financial institution of their choice.

- The accounts would not be integrated with Social Security and would not affect the worker's Social Security benefit. However, the account would be reserved for retirement and could not be accessed until the worker applies for Social Security benefits.

- Social Security's annual income would be enhanced through several provisions.
  - Beginning in 2030, the payroll tax rate would gradually increase in tandem with the program's costs. The total tax rate would increase from 10.4 percent to 13.7 percent by 2060.
  - The amount of wages subject to the payroll tax (currently $72,600) would increase relative to current law. Future benefits would increase accordingly for affected workers.
  - The taxation of Social Security benefits would be increased so that benefits are taxed in the same manner as defined benefit pension plans. Low-income workers who have no income tax liability would continue to be exempt from the taxation of benefits.
  - Newly hired State and local workers would be included in the Social Security program, thus imposing a payroll tax on their wages.

- Program costs would be contained through several benefit revisions.
  - COLAs would be reduced for all beneficiaries based on revisions to the CPI.
  - The already-scheduled increase in the normal retirement age from 65 to 67 would be repealed. However, the benefit formula factors would be indexed for life expectancy. This provision would not apply to young survivors or disabled workers.
  - The benefit computation period would be extended from 35 years to 38 years. This provision would not apply to disabled workers.

- KidSave Accounts would be created for all children born after January 1, 1995. The government would make a maximum $3,500 contribution funded with general revenues.

- The earnings limit would be reduced for all beneficiaries (age 62 and over.)

- The plan would reduce the CPI for all government programs and provisions indexed to the CPI except the SSI program.

Mr. SHAW. Mr. Houghton.

Mr. HOUGHTON. Yes, Nick, help me on the arithmetic a little bit. The major differences in the plans are the way they handle the funding of the gap. And some people, like Kolbe-Stenholm, they cut benefits. There are other plans that take money out of general revenues. Now I don't know how you slow down the benefit increase for high-income retirees and thereby pay for that gap. It doesn't seem like enough.

Mr. SMITH of Michigan. What it does is it adds another bend point. For those who are familiar with the way Social Security benefits are calculated, it is progressive because you start at the first roughly $500 and you get 90 percent back of your average monthly earning for everything under $500. Between $500 and $2,300, you get 32 percent back. Over $3,200 a month, you get 15 percent. I add another 5 percent bend point that is indexed at $3,700. That, over time, dramatically reduces fixed benefits for that individual

that has high earnings. We tried to set that $3,700 so that it matches what that individual might earn at about 6-percent return on what they are allowed to individually invest. The other thing that we do, Amo, is we take away the indexing of those bend points not for the 90 percent or the 32 percent, but for the 15 percent and the 5 percent, we index them to CPI or inflation rather than the current indexing based on wage inflation. Now the wage inflation, of course, is higher than the CPI. So we change that benefit calculation so that a growing economy actually has a greater positive result.

That is sort of a long answer.

Mr. HOUGHTON. Well, so what you are saying is that slowing down the benefit increase for the high-income individuals really does fill in the money for that gap without doing anything else?

Mr. SMITH of Michigan. That fills in a lot of the money for the gap. The other thing that we do is we index the ultimate retirement age to life expectancy. So we don't go over the 67 years that is now in current law, but we do speed it up like several of the other proposals.

Mr. HOUGHTON. Oh, I see, OK. Thank you very much.

Mr. SHAW. Anybody else seek recognition?

Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman. And, Nick, good to see you here and I know you have put a tremendous amount of work into this over the last several years and you have been tireless and relentless about coming forward with a proposal, and I want to congratulate you on the result of your work.

Mr. SMITH of Michigan. Thank you.

Mr. WELLER. One of the goals I think all of us have is the solutions for strengthening Social Security for next three generations are a bipartisan effort. Do you have any Democratic cosponsors?

Mr. SMITH of Michigan. No, I had one cosponsor in 1994, two cosponsors in 1996, six cosponsors in 1997, and I haven't solicited cosponsors yet this time. But I think it is important to try to get Democratic cosponsors. What I have learned, as chairman of the Task Force, Mr. Weller, is there seems to be some feeling that not moving ahead with a solution for Social Security might be a political advantage to somebody, sometime, somehow. I am sure this Committee has experienced some of the same considerations. But I do think ultimately there has got to be a bipartisan effort of some kind.

It is interesting researching the records when we started Social Security in 1934, the Senate on two votes insisted that there be allowed private investments, that that mandatory private investment that could be only used in the retirement should be an option to the fixed system. That lost out in conference Committee, partially I'm sure because of the Depression and the arguments of what might happen.

I do have a safety net in my bill that any individual that would be more conservative in their investments at age 60 on and invest not more than 60 percent in capital investments and 40 percent in stocks would have the security of a 95-percent protection.

Mr. WELLER. Mr. Smith, I just have a couple of questions here and I am one of those like you who believes the sooner we address

this problem, the better. And I am anxious that this Committee and this House and this Congress and this President act on it, hopefully this year. I think it is important that we move forward legislation. And, of course, it is going to take a bipartisan effort.

Just a quick followup on Mr. Houghton's question regarding gradually slowing down the growth of benefits for high-income retirees, could someone define that as means testing?

Mr. SMITH of Michigan. Well, except, Mr. Weller, it is offset by the additional earnings that that individual can make because we started at 2.6 percent, as I mentioned, of taxable payroll and it will eventually go up to 8.4 percent. But because that percentage of the $74,000 of taxable payroll is a lot more significant opportunity to get returns from the stock market, the means testing or making the formula distribution for the fixed benefits more progressive, that type of means testing is well offset by the increased investment opportunity because of the simple fact that they have more money——

Mr. WELLER. But if you are a high-income retiree, you receive less benefit?

Mr. SMITH of Michigan. No, no, actually, you would receive more benefits and that is with the assumption that you are going to have a real return above 4 percent interest. Any real return above 4 percent will give the high-income person more total benefits, because they have more interest growing their higher private retirement savings accounts. This is true even though there would be less in the fixed portion of the benefit program.

Mr. WELLER. The last question I want to ask, Mr. Smith, is under your proposal, it is my understanding you cover all State and local government employees hired after I guess beginning in 2001. And I have had kind of a continuous parade of police and firemen and others through my office concerned about being included in any Social Security plan. They prefer to be independent and have their own program. Can you explain why you believe that all State and local government employees should be included in the Social Security Program?

Mr. SMITH of Michigan. Well, I think part of it is the survivor and disability insurance portion of the program. The greater amount that we spread that risk around on the disability and survivor insurance, probably the better off we are as a country and the less chance to have something bad happen in a local community that is just simply buying that disability retirement insurance.

Mr. WELLER. For these police and firemen who have, of course, expressed opposition to being included, what is the benefit to them in being included as part of your program?

Mr. SMITH of Michigan. If there isn't a significant increase in disability or survivors benefits, then there would be no benefit to them. But there is a slight benefit to the rest of the system. Not too much but a little.

Mr. WELLER. All right. Well, thank you, Mr. Chairman. Thank you, Nick.

Mr. SHAW. Mr. McInnis.

Mr. MCINNIS. Thank you, Mr. Chairman.

Mr. SMITH of Michigan. Can I just add 0.21 percent out of the unfunded liability of 2.07 percent is satisfied by bringing the other States and counties in.

Mr. MCINNIS. May I proceed, Mr. Chairman? Thank you, Mr. Chairman. Mr. Smith, there are a couple of points. I am slow here but you talk about high income, but first of all, with due respect, I disagree with you that there is no tax increase in there. There is a tax increase in here for high-income people. If you don't cut their taxes but you cut their benefits, that is a proportion that has an increase impact on their tax. Somebody has to pay for this.

As I try to walk my way through your explanation to my good colleague, Mr. Weller, you said, "No, it cuts their benefits but really it is better for them because they get expanded investment opportunities so they actually make more." Who is paying for it? I mean this thing isn't free. Every time you are going to pay an additional dollar, that is a transfer. Somewhere that dollar has been created and to put it into your program at the amount especially that you suggest, it has got to come out of somebody's pocket.

Let me go through my questions first and then I will give you the last part to answer. So I haven't figured out how, I guess I am just not following your steps. And I don't exactly consider saying we are going to cut your benefits but we are going to give you more investment opportunities with your own money therefore you ought to be happier about it. Clearly, what it is to me is means testing. So the question I would have, the concluding question on this portion of my questions, is on the means test. Number one, what is high income under your category? What qualifies for that, what numbers? And, number two, do the people in that high-income bracket get back at least principal that they have put in under your plan? So if you would answer those questions, start there.

Mr. SMITH of Michigan. OK, I think maybe I am a little weak on my words when I use the word "benefit." I was applying the word benefit cut to the fixed portion of Social Security. So as you take the 12.4 percent, what I do in my bill, I set aside 4 percent for disability and survivor and so I never touch that 4 percent. The actual cost now I think is about 2.4 percent. So I take what is left starting at 2.6 percent and put it into a private investment account that is assumed by the actuaries to earn a real return of 7 percent. Eventually, the private investment portion is going to be greater, is going to give more benefits than the fixed portion of Social Security. So when I say that we are cutting benefits, we are only cutting the fixed Social Security benefits. For example, assume that the taxable income a few years from now is $100,000, so at that time in my bill 5 percent is allowed to go in a personal retirement savings account, 5 percent or $5,000 a year goes into that individual's account to invest and compound at 7 percent while their fixed benefits go down.

Since I add another bend point to the calculation of 5 percent, at $3,700 this year, that means anybody that has an average monthly income of $3,700 would fall into the next bend point and thus have a reduction in their fixed benefit portion of Social Security.

Mr. MCINNIS. So you consider wealth anything below say $45,000 a year, they are considered high income above that?

Mr. SMITH of Michigan. At least higher income. But here again, consider the total benefits, their personal retirement investments and their government-paid benefit. If you are making $20,000 and you are allowed to invest 5 percent of it, you can invest $1,000 a year.

Mr. MCINNIS. Let me reclaim my time since we are in the yellow so very quickly because then it still doesn't—what Mr. Houghton, my good colleague questioned you about, is that difference is what you rely on totally to carry the costs of this plan. And I just cannot picture where you are going to come up with that kind of block of funds as a result of slowing down the growth of benefits while giving these people additional opportunities?

Mr. SMITH of Michigan. Well, the actuaries specifically and you have an actuarial——

Mr. MCINNIS. Let me point out one other thing and then I will reclaim my time and then I will yield to you for the balance and that is that I don't consider $45,000, that is rounded off, I don't consider $45,000 a year high income. It is certainly not high income in the area I am in.

Mr. SMITH of Michigan. I think I will change my words to say higher income rather than high income. But the opportunity of what you are going to gain on your private investment more than offsets your fixed benefits reductions.

Mr. MCINNIS. Thank you, Mr. Chairman.

Mr. SHAW. By just being able to put everything in the record that really should be with regard to your plan, the Social Security Administration communication dated June 5, 1999, which I assume you probably have received copies of, they point out that the transfers, this is on page 3 of that communication: "The transfers from the General Fund of the United States Treasury would be required for the years 2001 through 2009 with the amount specified in law as $11 billion for 2001, $59 billion for 2002, $51 billion for 2003, $68 billion for 2004, $79 billion for 2005, $116 billion for 2006, $134 billion for 2007, $146 billion for 2008, and $165 billion for 2009. These amounts are based upon the current estimates by the Congressional Budget Office of the amount of on-budget surplus for these years." I don't put that out to be critical because the Archer-Shaw plan also requires some revenue coming into it in the years commencing about 2015.

Mr. SMITH of Michigan. Clay, what we did is I ran into a lot of brick walls increasing the retirement age to 69. And so I was looking for a way to do away with that increase in retirement age and what we did to accommodate that was use the amount of the Social Security Trust Fund surplus in terms of not having General Funds support not to exceed the Social Security Fund surplus for those years that allowed me not to increase the retirement age.

Mr. SHAW. I think that was a wise decision. It is very difficult to think about blue-collar people, or at least a majority of them continuing to work beyond the current retirement age. I want to compliment you. You have been involved in this longer than I have, I might say. And I know you have done a lot of work and you have thoroughly examined the subject, and I appreciate your being here with us and testifying this afternoon and outlasting everybody just about.

Mr. SMITH of Michigan. Well, anyway, thank you, Mr. Chairman.

Mr. SHAW. And I know that you also had another obligation to chair a Committee and that makes it even more special that you see your obligation here and you certainly have fulfilled it well. And thank you for testifying.

Mr. SMITH of Michigan. Thank you.

Mr. SHAW. And this hearing is now adjourned.

[Whereupon, at 4:28 p.m., the hearing was adjourned.]

PROPOSALS CERTIFIED TO SAVE SOCIAL SECURITY

THURSDAY, JUNE 10, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, DC.

The Committee met, pursuant to notice, at 10:07 a.m. in 1100 Longworth House Office Building, Hon. Bill Archer (Chairman of the Committee) presiding.

Chairman ARCHER. The Committee will come to order.

Good morning. Now that things have cooled off outside, we have a good environment to continue to consider Social Security and to, at least for the time being, complete our hearings.

Today the Committee will continue what we started yesterday in evaluating and hearing about plans that save Social Security for the required 75 years. I hope all the Members of the Committee agree with me that yesterday's hearings were productive and constructive in helping us to understand what the various options are.

All of the plans presented yesterday, in my opinion, were positive and good contributions to the debate. And I again congratulate those Senators and House Members who participated in the hearings.

Very soon this morning I will take the witness stand with Social Security Subcommittee Chairman Clay Shaw to present the Archer-Shaw Social Security Guarantee Plan to the Committee. But before I do, I feel constrained to say that I believe I have upheld my end of the deal.

My friends in the Minority said, present a plan, and I did. The President asked me, when I met with him, to reach out and include the Minority, including the Minority Leader, and I have. The President and many Democrats on the Committee said that we should hold hearings, and we are.

And I am committed to continuing our bipartisan effort on Social Security. And this morning I announce that if the Minority agrees, I will schedule executive sessions for the Ways and Means Committee to discuss areas of common ground and a potential legislative outline for markup.

In that same bipartisan spirit, I hope that the President will meet with the Ways and Means Republicans as soon as possible, just as he has already met with the Ways and Means Democrats on the Committee.

I believe that will help to move the process forward.

And clearly, the President's leadership is vital to the ultimate solution of this problem. Each one of us, each Member of the Con-

gress of the United States and the President of the United States, must examine his and her conscience and determine whether they truly want to solve this problem this year or whether they are motivated by other reasons. And only each Member can answer that question.

I hope that each Member will recognize how important it is to do this job now. Waiting will only make it more difficult in increasing percentages. The options are before us now, and now is the time to choose from them and to move forward because now is the best opportunity that we will ever have to strengthen and to save Social Security.

As the President said early on, once in a blue moon we have this opportunity, and it is now ours to reach out and to grasp and to prove that we can meet the challenge.

The American people expect this of us. They know that it is vital to all Americans, and they know it needs to be saved and that the job needs to be done now.

We have the opportunity to prove something that is truly historic. It is not easy. But we can prove that a democracy can address a difficult problem far in advance of the drop-dead date. We can prove that perhaps for the first time that we don't have to wait until we are at the edge of the cliff. Because if we wait until we get to the edge of the cliff, the options will be very limited. They will be to cut benefits or raise taxes.

I think each of us owes a responsibility to every generation in this country and to generations to come. Social Security should be intergenerationally fair.

Now, in my opinion, that means that taxes on our grandchildren when they are in the prime of their work life should not be any higher than we are paying today. It also means that the benefits that they will receive when they retire, having paid an equal amount of taxes, will be the same as we are receiving today, those of us who are retired.

That is a great challenge. But every month, as I look on my 13 grandchildren, I know that I care. I will be gone, but they must be considered.

To do it in any other way is not right. In fact, it is wrong. Any program that would increase taxes on our grandchildren and reduce their benefits is wrong. And I hope all of us will be motivated by that same spirit.

With that, as I said yesterday, I am looking forward to enjoying the fun that every witness has in being interrogated by the Members of this Committee. [Laughter.]

I guess I look at this moment very sentimentally on this Committee. I have served on it since 1973, and next year will be my last year. And I will miss every one of you, whether you be Democrat or Republican. This is the greatest Committee in the greatest legislative body in the world.

And I know that we will shoulder our responsibilities on the major issue facing all Americans today and during the next century.

And I yield to my colleague Charlie Rangel for any comments he might wish to make. [Applause.]

[The opening statement follows:]

Opening Statement of Hon. Bill Archer, a Representative in Congress from the State of Texas

Good Morning. The Committee will come to order.

Today the Committee will continue the hearing we started yesterday on plans that save Social Security for 75 years.

I thought yesterday's session was very productive, and I think it shows specifically the options available to us as we move forward to save Social Security. All of the plans presented yesterday were positive contributions to the debate, and I would again congratulate those Senators and Members of Congress who participated.

I will soon take the witness stand with Social Security Subcommittee Chairman Clay Shaw to present the Archer/Shaw Social Security Guarantee Plan.

But before I do, let me say one thing: I've upheld my end of the deal.

My friends in the minority said present a plan—I did. The President asked me to reach out and include the minority, including the minority leader—I have. Democrats on this Committee said hold hearings on Social Security—we are.

I am committed to continuing our bipartisan effort on Social Security, and today I announce that if the minority agrees, I will schedule executive sessions for the Ways and Means Committee to discuss areas of common ground and a potential legislative outline for markup. In that same bipartisan spirit, I would request that President Clinton meet with Ways and Means Republicans as soon as possible for the same purpose. Just as the President has met with Ways and Means Democrats on Social Security, so too should he meet with Republicans in order to keep this process moving forward in a bipartisan fashion.

The options are before us, and now is the time to choose from them and move forward. This is the best opportunity chance we'll have to strengthen Social Security for some time. Each day we put this off the tougher the job becomes. And most important, the American people expect and deserve for us to act now.

With that, I greatly look forward to hearing from our next panel, and I would encourage Committee Members to give an extra special amount of respect and courtesy to them.

Mr. RANGEL. I started to say Mr. Chairman—and I say that out of respect—but I feel more comfortable saying Bill, that was a very moving speech because we all share the same love for this Committee and this great body that we are privileged to serve in. I have said before, and I truly believe, that as the next election comes upon us that we don't need Social Security out there to be what we campaign for or against. There are enough differences, and I mean honest and serious differences between our parties in dealing with the problems that we face as a Nation to have a good contest in November.

I think that it would enhance the respect and support of both Democrats and Republicans, and the House as a whole, if we could come together in a bipartisan way and give you and our President and our Nation, of course, a bipartisan Social Security bill.

In your very moving remarks, the one thing that I think deserves particular attention is your suggestion that we go into executive session, which, in my opinion, is the only way to see how much we can accomplish as a Committee. Of course, we would want to do this with the President's people being aware of the direction in which we are going to make certain that if we come near a solution that it is going to be acceptable to the administration.

I think our hearings are good as a beginning and as an educational vehicle, since I think the American people are not necessarily aware of the serious nature of the problem in the outyears.

It is true that, as you take the witness stand, the cloak of Chairmanship will be removed from you. It is also true that we intend

to give the same scrutiny to the proposal that you and my friend Clay Shaw have come up with, as you have given to our President's proposal.

But we are only dealing with proposals at this stage so that there will be no personal setbacks for anybody because even the Republican leadership has not embraced your proposal, just as Democrats have not embraced the President's proposal.

I really am moved by you calling for the President to provide leadership on this, because on other legislative issues I have not heard the same request that we have to hear from the President as we legislate. I think what you mean, but didn't say, is that we can't get anything accomplished on this issue unless there is bipartisanship. The President has to be a part in creating that climate of bipartisanship.

Nonetheless none of us are thinking about giving up our legislative responsibility to a task force or to the President.

Now, having said that, any critique or analysis of the proposal which you have drafted should only be taken in the same spirit in which we have critiqued the President's proposal, and with the understanding that the serious business will have to be done by trying to find out, not how far apart we are, but how close we are that will give us the basis of going into executive session with experts to see whether or not those differences can be closed and whether we can bring something to the floor.

Now, as Charlie Stenholm said yesterday, any proposal can be picked apart, because somewhere along the line it has to be paid for. We have a tendency politically just to talk about the pain in paying for things, but paying for things is not nearly as painful if we were to create a package which showed that we protected the integrity of the system for the next 75 years.

I don't know why you have moved me at a time you are going to be sitting in the witness chair, but as always, I will be kind and hope it is well respected, Bill.

I want to tell you that I know you are going to miss this House. There has been no Member that I have known that has been more dedicated and that has done more to protect the integrity of this Committee. We don't know who will be sitting in your chair in the next session, but certainly we know that the dignity and integrity and respect that you brought to it will have to be maintained.

Thank you.

Chairman ARCHER. I thank the gentleman for his comments.

And with that, I turn the gavel over to the Ranking Republican on the Committee, Mr. Crane.

Mr. CRANE [presiding]. Well, let me welcome our witnesses to the Ways and Means Committee. You have had virtually no experience sitting where you are.

Mr. SHAW. It is an intimidating view from here, I would say. [Laughter.]

Mr. CRANE. But I would like to welcome the commencement of the testimony of our first witness. I believe you are from Texas, aren't you, Chairman Archer?

Chairman ARCHER. Yes, sir. Proudly.

Mr. CRANE. Chairman Archer first. [Laughter.]

STATEMENT OF HON. BILL ARCHER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS; AND CHAIRMAN, COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES

Chairman ARCHER. Chairman Shaw, it is a little intimidating to be down here. And I must say that I feel a little bit like Pickett at Gettysburg. But we shall proceed.

As I mentioned earlier, I think we have a historic opportunity this year to save Social Security. And today I present to the Committee the details of the Social Security Guarantee Plan, which Social Security Subcommittee Chairman Clay Shaw and I have unveiled in April.

We followed four basic principles as we crafted this plan. First, we needed to save Social Security for 75 years. That is probably not long enough. We should be able to project that the saving and strengthening will extend beyond the 75 years as best we can project today, if, in fact, we are going to say to younger generations, yes, you can have confidence in what we are doing for your future.

Second, we do not raise taxes, and we do not cut benefits. Social Security as we know it today will be available to generations to come in the next century. Third, we maintain the safety net for workers, and fourth, we provide new options for younger workers.

First and foremost, our plan saves Social Security for as far as we can see. And I believe that is a critical benchmark.

I hope all of us on this Committee will not lose the focus of why we are here today. We would not be here at all today if we did not project that Social Security would be unable to meet its obligations in the next century. We would not be here talking about an awful lot of adjuncts, an awful lot of changes in the program, which you heard in many of the presentations yesterday, were it not that Social Security was going to go into default.

And so I believe our focus should be—and Clay Shaw agrees and that is one of the major things we thought about as we put this plan together—and should never be lost, to maintain the current Social Security system on a realistic basis over the next 75 years.

The Chief Deputy Actuary for the Social Security Administration is here today, and I believe he would agree. And if I might digress momentarily, he and his staff deserve enormous compliments from all of us because they have worked untiringly under enormous time pressures over the past couple of weeks in order to evaluate the programs that were submitted to them. And I personally want to give the highest commendation to Steve Goss and all of the people who work with him. [Applause.]

We all know that it is relatively easy to save Social Security for 20 or even 30 years. In fact, the current projections of the Social Security actuaries are that the benefits will be paid in full through the year 2035. And so why worry today?

But we know that the demography is going to change so dramatically in the next century that we better worry today or the solutions will become virtually impossible. The financial reality of dealing with the system over the long term is our greatest challenge. And as I said yesterday, 75 years is the average life of a worker, or it was. And that is expanding. So perhaps in the future, actu-

aries will feel that they need to extend that to 80 or 85 years to accommodate the advances in medicine and nutrition and other things we are providing to our population. But we owe it to be honest with future generations.

Second, our plan fully preserves the current Social Security system, including COLAs, and fully protects its benefits. If you don't believe me, let me share with you the words of Congressman Earl Pomeroy, the cochairman of the Democratic Task Force on Social Security, who said the following about our plan, and I quote: "It would preserve the Social Security Trust Fund for Social Security. It would preserve the guarantees represented in the present Social Security Program. No one would do worse in the next century, and each would be guaranteed at least as much benefit as they have under the current existing program," end of quote. Now that is a key difference between our plan and some other plans that you heard about yesterday, no benefit cuts.

As we discussed yesterday, AARP views COLA cuts and increases in the retirement age as benefit cuts. And I am glad to say that the Archer plan has neither. And as I mentioned yesterday, any legislated reduction in the COLA, in the CPI, will also be a tax increase heavily distributed on middle-income Americans.

Again our plan guarantees Social Security benefits for all workers. It doesn't matter if you are 65 or newborn, our plan guarantees that you will receive at least the amount promised to you under current law.

Now here is how it works: In short, our plan modernizes Social Security's financing to prefund the benefits and gives workers the opportunity to create real wealth for themselves and their families. The Archer-Shaw plan would save Social Security by giving millions of American workers a tax cut equal to 2 percent of their earnings to create their own Social Security Guarantee Account.

This is a tax cut that I believe everyone on a bipartisan basis can support. And the distribution tables are remarkable because almost two-thirds of the benefit goes to people with under $50,000 a year of income. That should appeal to people on both sides of the aisle.

Furthermore, each dollar of tax cut represents one dollar of personal savings, which this country desperately needs. Today, our personal savings rate is at the lowest of all time in the history of this country and threatens the very thriving economy that can be seen in the future.

Upon retirement, a beneficiary will receive his or her full Social Security check, or a greater amount, depending on the balance of their Social Security Guarantee Account. And this guarantees that each and every American will receive at least his or her Social Security benefits forever, or at least as far as we can see.

But our plan does even more. We include an inheritance feature so that if workers die before they retire, their accounts could be passed tax free to their heirs, something which the current system prohibits.

We also completely eliminate the unfair earnings limit that penalizes working seniors who either have to work or want to continue to work and risk the loss of their Social Security benefits. This is a feature that in my opinion has been wrong in the law.

And I am excited that the President has stated his strong support for eliminating the earnings limit.

Plus, our plan includes, which I don't believe any other plan presented to us yesterday offers a feature that should appeal to all small business people and to all employees, all workers in this country. And that is a reduction in the payroll tax of 4 percent, while still safeguarding the trust fund.

Finally, the Archer-Shaw Social Security Guarantee Plan pays for itself. Even under the most conservative estimates, the Social Security Guarantee Plan will result in a net Federal budget surplus over the next 75 years.

And before turning to Chairman Shaw, let me point out some very significant differences between our plan and Mr. Stark's plan. Not to single you out, Pete, but you were the lead-off witness.

The Archer-Shaw plan would immediately boost significantly the personal savings rate in the country, which is currently at a negative 0.6 percent. Number two, the Archer-Shaw plan would result in net Federal budget surpluses. Number three, the Archer-Shaw plan would cut payroll taxes by 2½ points in 2050, and 1 percentage point in 2060. Number four, the Archer-Shaw plan would eliminate the senior work penalty on earnings. And number five, the Archer-Shaw plan would back Social Security benefits with real assets, not just IOUs.

The most significant difference though is that our plan has the backing of the Chairman of the Ways and Means Committee, or so I have been told. [Laughter.]

And I now yield back my time, if there is any left, Mr. Chairman.

[The prepared statement follows:]

Statement of Hon. Bill Archer, a Representative in Congress from the State of Texas; and Chairman, Committee on Ways and Means, U.S. House of Representatives

We have an historic opportunity this year to save Social Security. And today, I want to share with you the details of the Social Security Guarantee Plan, which Social Security Subcommittee Chairman Clay Shaw and I unveiled in April.

We followed four principles when we crafted our plan.

1) Save Social Security for 75 years.
2) Do not raise taxes or cut benefits.
3) Maintain the safety net for workers.
4) Provide new options for younger workers.

First and foremost, our plan saves Social Security for 75 years, which I believe is a critical benchmark. The Deputy Chief Actuary of the Social Security Administration is here today, and I think he would agree. We all know it is relatively easy to save Social Security for 20 or even 30 years, but the financial reality of dealing with the program over the long-term is our greatest challenge. As I said yesterday, 75 years is the average life of a worker. We owe it to future generations to be honest with them.

Second, our plan fully preserves the current Social Security system—including COLAs—and fully protects its benefits. If you don't believe me, let me share with you the words of Congressman Earl Pomeroy, the Co-Chairman of the Democrat Task Force on Social Security, who said the following about our plan: "It *would preserve the Social Security Trust Fund for Social Security*. It would preserve the guarantees represented in the present Social Security program. No one would do worse, you'd be guaranteed at least as much benefit as you have under the existing program."

That's a key difference between our plan and some other plans—no benefit cuts. As we discussed yesterday, AARP views COLA cuts and increases in the retirement age as benefit cuts. I'm glad to say the Archer/Shaw plan has neither. Again, our plan guarantees Social Security benefits for all workers. It doesn't matter if you are 65 or newborn, our plan guarantees that you will receive at least the amount promised to you under current law. Here's how it works:

In short, our plan modernizes Social Security's financing to pre-fund benefits and gives workers the opportunity to create real wealth for themselves and their families.

The Archer/Shaw plan would save Social Security by giving millions of American workers a tax cut equal to 2% of their earnings to create their own Social Security Guarantee Account. *This is a tax cut that everyone can support.*

Workers would then select where to invest their SSGA fund. The assets in these accounts would grow tax-free. No withdrawals would be permitted until a worker became eligible for either retirement or disability benefits.

Upon retirement or disability, a beneficiary would receive his or her full Social Security check, or a greater amount, depending on the balance of their Social Security Guarantee Account. This guarantees that each and every American will receive at least his or her Social Security benefits—*forever.*

But our plan does even more. We include an inheritance feature so that if workers die before they retire, their accounts could be passed tax-free to their heirs, something the current system prohibits. We also completely eliminate the unfair Earnings Limit that penalizes working seniors. Plus, our plan includes a gradual reduction of payroll taxes so that government can't grow bigger at Social Security's expense.

Finally, the Archer/Shaw Social Security Guarantee Plan *pays for itself.* Under even the most conservative estimates, the Social Security Guarantee Plan will result in *net federal budget surpluses* over the next 75 years.

Before turning to Chairman Shaw, let me point out some very significant differences between our plan and Mr. Stark's plan:

1. The Archer/Shaw plan would immediately boost the personal savings rate—currently at negative 0.6%.
2. The Archer/Shaw plan would result in net federal budget surpluses.
3. The Archer/Shaw plan would cut payroll taxes by 2.5 percentage points in 2050 (from 12.4 to 9.9 percent) and 1percentage point in 2060 (to 8.9 percent).
4. The Archer/Shaw plan would eliminate the senior work penalty on earnings.
5. The Archer/Shaw plan would back Social Security benefits with real assets, not IOUs.

Mr. CRANE. Thank you, Mr. Witness.

And our next witness is Mr. Shaw.

But may I remind our witnesses to please try to keep your oral testimony confined to 5 minutes or less, and any additional material will be made a part of the permanent record. [Laughter.]

Mr. RANGEL. Mr. Chairman. I ask unanimous consent that these witnesses have as much time as they think is necessary in order to present their views. [Laughter.]

Mr. CRANE. Hearing no objection, so ordered. [Laughter.]

STATEMENT OF HON. E. CLAY SHAW, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. SHAW. Mr. Chairman, I have a full statement that I would ask to be placed in the record. And I will summarize as I think Chairman Archer has very adequately described our Social Security plan to the Committee.

There are just a couple of things that I think that I would like to underscore, which I think is something that this Committee should take a close look at. When I was first asked to take the reins of the Chair of the Social Security Subcommittee, I made a decision, which I haven't really talked that much about. But I thought at that point that that would probably be the end of my career in this Congress in that I represent a very senior district of south Florida.

I did not realize until I got into the matter and started really looking at the solutions, not just the problems. The crisis I always

knew about, and I think every Member of this Committee knows that there is a crisis pending out there that is going to really nail our kids and our grandkids.

But I didn't realize that we could solve the problem of Social Security without touching Social Security. And I think that is what every Member of this Committee should certainly look at. What we have been able to accomplish, if the Archer-Shaw Social Security reform bill is passed and becomes law, is we have preserved Social Security in its existing form for all times.

FICA taxes will remain, at least for the time being, at present levels, and they will be invested as they are today, entirely in Treasury bills. None of the FICA taxes are going into the stock market. Every benefit that is presently existing, including today's COLA, is preserved. We don't meddle with that at all.

So Social Security as it is today is not being touched. What we have done, instead of going the route of a carve-out, which would take FICA funds out of the Social Security Trust Fund, we have established individual retirement accounts for American workers.

Can you imagine the opportunity that we have as Republicans and Democrats to come together and give, perhaps, the largest tax cut to all American taxpayers, including some of those who don't pay taxes, by a refundable tax credit and for the first time give millions of low-paid American workers the opportunity to accumulate personal wealth in the form of an individual retirement account? This is quite incredible. And it is something that we can come together as Republicans and Democrats and accomplish.

For the first time, so many workers in this country who have been left behind and have never been able to even have a hope of accumulating something of their own will have that opportunity. Yes, if they choose to retire, and when they choose to retire, that individual retirement account will have to go and be annuitized through the Social Security Administration.

But so many workers today who die before they retire lose every penny that they have put into the Social Security system, particularly minority workers today who go into the work force at an earlier age and die at an earlier age. Instead of losing every dime that has been paid to the Social Security system by themselves and by their employers, they will have something that they can leave to their heirs.

This is a tremendous, significant, and very, very fair situation. And we have brought them into being able to enjoy part of the American dream. I think it is an incredible program, and I think it is one we should be able to embrace.

I think the Chairman and I are certainly open to any suggestions that you might have. As was pointed out by Mr. Rangel, this has not been embraced as the Republican bill. And I think it is one that has to be done, not as a Republican bill. I don't think we can pass a Democratic bill either.

I think what we need to do is to come together with a bipartisan bill. And I think we need to bring along the leadership of both parties.

Now, Mr. Rangel, you asked the question why the President isn't called on to provide leadership on other types of legislation. Other types of legislation have more of a partisan nature to it than this.

This is one for all American workers, Democrats and Republicans. This isn't rich versus poor. This isn't spending versus tax cuts. This is something that all of us need to work together and be able to accomplish.

And I look forward to your questioning.

Thank you.

[The prepared statement follows:]

Statement of Hon. E. Clay Shaw, Jr., a Representative in Congress from the State of Florida

Today 44 million Americans—one in six—depend on Social Security retirement, disability, or survivor benefits. But because Americans are having fewer children, living longer, and retiring sooner, Social Security's financing system faces trouble ahead. As Social Security's Trustees told us in their most recent annual report, this problem will become acute after 2014 when Social Security spends more on benefits than it takes in through taxes. If we want to keep the budget balanced and pay all the benefits seniors are promised, other government spending will have to fall or taxes will have to rise or government debt will have to increase by no later than 2034—not just for retirees then, but for their children and grandchildren as well.

That is, if we fail to act.

That is why Chairman Bill Archer and I have proposed the Social Security Guarantee Plan to permanently save Social Security by creating real savings for Americans' retirement security. As the Social Security Administration's independent actuaries stated, the Guarantee Plan "would be expected to eliminate the estimated long-range OASDI (that is, Social Security) actuarial deficit...allowing timely payments of benefits in full through 2073, and beyond."

We crafted this plan to achieve four key goals: (1) no payroll tax hikes; (2) no benefit cuts; (3) no direct government investment in the private financial markets; and (4) save Social Security for 75 years and beyond.

That is why the Guarantee Plan ensures fairness by rejecting payroll tax hikes, by rejecting increases in the retirement age that would unfairly burden our children and grandchildren, and by rejecting COLA cuts that would harm seniors and especially women. Our plan also protects workers' rights by eliminating the Social Security earnings limit and making sure their Social Security taxes are protected and not spent on other Washington programs. That's the strongest lockbox ever. Our plan promotes fiscal responsibility by backing Social Security benefits with real wealth instead of IOUs for the first time. For the economy, the benefits are clear as well: by 2074, this plan will have increased net national savings by a total of \$15 trillion (in 1999 dollars), spurring economic growth, generating new jobs, and promoting budget surpluses. And in addition to fully protecting *all* current benefits and even creating new benefits for workers and their families, our plan dramatically reduces payroll tax burdens on our children and grandchildren in the long run.

As its name implies, the Social Security Guarantee Plan is designed to guarantee that full uncut Social Security benefits are provided to all beneficiaries today and in the future. This proposal does not affect Social Security benefits in any way. There is no individual risk—everyone is guaranteed their current Social Security benefits, regardless of the market returns on their individual accounts.

The U.S. General Accounting Office has told Congress that to save Social Security, payroll taxes would have to be raised by 15 percent or benefits cut by 13 percent immediately. (To put that in perspective, for the average retiree receiving about \$750 per month in benefits, if we relied on benefit cuts alone to maintain Social Security's soundness we would have to reduce monthly benefits by about \$100, to \$650. Obviously, that must be avoided at all costs.) If we delay, even more drastic benefit cuts or tax increases would be needed to keep Social Security up and running. The Social Security Guarantee Plan answers this challenge of saving Social Security without raising payroll taxes, without cutting benefits, and without direct government investment of Social Security Trust Funds in private financial markets.

Here's how the Social Security Guarantee Plan would work. Each worker covered by the Social Security program would receive an annual tax credit equal to 2 percent of his or her earnings (up to \$72,600 this year). So if you make \$20,000 you get a \$400 tax credit; if you make \$40,000, you get a \$800 credit; and the maximum tax credit would be \$1,452 (2 percent of \$72,600). This amount would be automatically deposited into a new Social Security Guarantee Account created for each worker. The worker could then select from among a broad range of savings and investment options for his or her Guarantee Account. Account balances would accumulate tax-free until retirement or disability. Once workers begin drawing Social Security

benefits, their Guarantee Accounts supplement funds from the Social Security Trust Fund to provide full Social Security benefits. If investment returns outperform historical averages, workers and their families could receive even larger benefits than promised today. In addition, many survivors may get higher benefits than current law provides because our calculation for survivor benefits under the accounts is more generous than current law. Plus our children and grandchildren will benefit from payroll tax cuts of up to 3.5 percentage points—almost 30 percent below today's rate.

If workers die before retiring, Guarantee Accounts pass tax-free to their children or grandchildren or other heirs, after making sure that their survivors receive all the benefits they are owed today. That's in contrast with today's Social Security in which workers can spend a lifetime paying taxes, die before retirement, and still not have savings to pass on to their family or heirs. So in addition to our main goal of saving Social Security for everyone, this plan for the first time creates real wealth for all workers they could leave to their families. Again, that's on top of keeping our commitment to provide full monthly benefits to workers, their widows and children.

Even current retirees would benefit by this plan in several ways. First, Social Security will be financially sound for 75 years and beyond under this plan; as Social Security's Trustees have stated, that is not the case today. Second, the Guarantee Plan would maintain Social Security's soundness *without touching Social Security's critical inflation protections (that is, without cutting cost-of-living adjustments or COLAs)*; as we have heard other plans call for COLA cuts. Finally, the Guarantee Plan increases and ultimately eliminates the current limit on how much retirees can earn without experiencing cuts in their Social Security benefits. So anyone who wants or has to work to supplement their Social Security can do so without being penalized.

Social Security is one of the greatest things about America, and we all want to keep it that way. Fortunately, the Guarantee Plan shows that Social Security can be saved without cutting benefits or raising payroll taxes. But we have to act and act soon or the task will get only tougher and the solutions more painful with each year that we delay.

Mr. CRANE. We thank our witnesses for their testimony.

I would now like to yield to our distinguished Ranking Minority Member, Mr. Rangel.

Mr. RANGEL. Clay Shaw, if you knew that this was going to have to be bipartisan if it was going to be successful, why were no Democrats asked to participate in this, for lack of a better word, this proposal that ultimately came from your task force?

Mr. SHAW. I think both of us in both political parties stood back for a long period of time, waiting for the others to take the first step. The President himself at the White House conference told us specifically. And you were there, I was there, Chairman Archer was there. He said he didn't expect the Republican Majority to come forward with a program, that he wanted to come forward with it.

He did come forward with a partial program in his State of the Union Address; however, nothing is out there yet from the White House that saves Social Security for all time. You can view this as a working document. The Chairman has said that he wants to have executive sessions, which I assume from your remarks that you accepted his offer to do that.

This is a proposal that is on the table. This is a working document. This is work in process. None of us has closed the door to further suggestions. And if this bill can be improved upon, both Chairman Archer and I would relish the opportunity of working with the Minority party in accomplishing that.

Mr. RANGEL. In the spirit of just trying to set some guidelines—because I do welcome executive session on this and other sensitive

issues where we all have to bite the bullet—and just trying to establish what we would be going into this session with, we are in the process now of trying to put into legislative form the President's recommendations. We are prepared to do it hoping to get the support of the President, but we feel a responsibility as legislators to introduce a bill.

Is there any way that we would know before we went into executive session whether your proposal has any support with Republicans on this Committee, on the floor, or with the Republican leadership? Because in order to put all of our cards on the table, we will be reporting to the Democratic Caucus what I consider to be progress in that executive session. They will be asking whether or not our leadership is talking with the Republican leadership. If you followed the day-to-day calendar, the legislative calendar, you will see that it's very partisan.

Of course, we are trying to say we want to make Social Security different, as you eloquently pointed out, from other legislation.

What kind of indication have you already received from your leadership that they are willing to work out a bipartisan agreement? Have they discussed this with the Democrats at all?

Mr. SHAW. I can't speak as to—I would defer to Chairman Archer as far as the conversations with leadership. However, I can tell you that I think the Speaker himself would like to move some legislation forward. I think that they are anxiously waiting for some signals from the Minority party that this legislation should be moved together.

I can tell you, without speaking for each individual Member of this Committee on the Republican side, I feel that the consensus certainly favors moving something forward. And I think the consensus also would favor something in the form of the Archer-Shaw bill.

Chairman ARCHER. If I may, let me just jump in briefly. I introduced into the record yesterday a letter from Speaker Hastert which supports our ongoing process of trying to find a solution to Social Security. He has strongly encouraged me to pursue attempting to find a bipartisan solution to Social Security. And in the meetings that I had with our leadership, at least the top part of our leadership, that same encouragement has existed.

And, like you, you are not ready to jump in and embrace the Archer-Shaw plan at this moment, although we would be happy to have that tomorrow, they are not jumping forward and saying this plan is the ultimate answer to the problem.

We have got to work through this process, but they are strongly supportive of finding the answer and strongly encouraging of the process that we are conducting right now.

Mr. RANGEL. Well, let me say this: the area that we do agree on, and unfortunately I haven't gotten to the substantive questions, is that we are not going to rush into this only to find out that it is just Clay Shaw and Bob Matsui and me and you. Most of the Members on this Committee, and Members of the House from both sides of the aisle, want to make certain that they have something that they can be proud of. If they are going to be hit and criticized, they have to feel comfortable that they have accomplished something for the years ahead.

I agree with you that the President has a responsibility to create the atmosphere that this not become a campaign issue in 2000. But it also seems to me that our leadership, both the Speaker and the Minority Leader, have a responsibility to make sure that this issue isn't so sensitive that they can't come together to talk about it or that they can't issue a statement to create an atmosphere where we can go into executive session knowing that we are not spinning our wheels.

I appreciate the fact that you are talking about executive session, and I will do all I can on my side to encourage a reaching out, but I know that you agree, Chairman Archer, that, if we are going to make history instead of political points, we have to have everyone onboard, not on the solution, but on the spirit in which we are working together toward that solution. While I haven't dealt with the substance of the bill, I think we have accomplished a lot in terms of the fact that at least we are talking publicly, even though I was a little disappointed that C-Span didn't show up this morning. [Laughter.]

But I look forward to whatever meetings we can have before the executive meeting so that the executive meeting, even though not programmed, can go as smoothly as possible.

I thank you. You have made pretty darned good witnesses, both of you.

Chairman ARCHER. And, Charlie, I would refer you to the letter that was entered in the record from the Speaker yesterday which I think will answer some of your questions. And if you don't have a copy, we'll get a copy to you.

Mr. RANGEL. I don't think there is any substitute, Mr. Chairman, for talking to each other. I mean, I am certain I can persuade Minority Leader Gephardt to have a profile in courage and issue a letter, but I don't think there is any substitute for our leaders breaking the trend that this session has started and talking with each other about what they would like to see us as a Committee do.

Mr. SHAW. Charlie, let me just add one thing to what you have said. At this point, this is not the Republican bill. And as a matter of fact, if you care to endorse it at the end of the day, this would become the bipartisan bill.

So I think that it is not a question——

Mr. RANGEL. It is not a Democratic bill either, but my point is, Clay, is that you have got to talk with people. I think we are OK. I think we made a giant step forward because I think a lot of Republicans and Democrats would just as soon this didn't come up.

What I am saying is that—I am not asking the Minority Leader and the Speaker to come up with a program. I am just talking about creating an atmosphere. Sooner or later, you and Bob Matsui will be talking to each other—sooner or later.

Mr. SHAW. Well, we are, Charlie. We are talking. You are talking to Bill; I am talking to you; I am talking to Bob Matsui. We are coming together. We are making progress.

And I think what Chairman Archer has indicated this morning, that let's expand this to the Full Committee.

Mr. CRANE. Mr. Houghton.

Mr. HOUGHTON. No questions.

Mr. CRANE. Mr. McCrery.

Mr. McCrery. Thank you, Mr. Chairman.

Chairman Archer, most, in fact, I guess, if there are no benefit cuts, all of the magic to your proposal really is in the individual accounts in allowing people to get a higher rate of return on 2 percent of their payroll taxes. Is that essentially correct?

Chairman Archer. Absolutely. And if I may, just very briefly, tell you that there is no magic to any of these plans that we heard from yesterday. But if you start with the premise of a triangle, and on one side of that triangle is that benefits are not going to be cut, and on the other side taxes are not going to be increased. And the bottom part of the triangle would be that you are going to save Social Security for 75 years. Then you must do two things.

You must rely on General Treasury funds to some degree. Now, frankly, I have a problem with the infusion of general Treasury funds directly into the Social Security Trust Fund. That violates the whole contract concept that has been established over history. But that is just my own personal view.

Others share it; some do not.

But recognizing that, what is the least amount of general Treasury funds that you can consume in order to be able to accomplish the goal of saving Social Security, which again is the focus we cannot lose. And second, you have to use the compounded returns of the private sector, which we heard a lot about yesterday from both Phil Gramm and Bob Kerrey and others who testified before us yesterday.

And that is what we do.

Mr. McCrery. Well, my question is, why only 2 percent. If we get such great returns from investing 2 percent, why not do 3 percent or 4 percent?

Chairman Archer. Well, because, for everything you gain, you give up something. You give up an additional loss to the unified budget surplus by taking more money out of the general Treasury.

And we did it with a minimum amount that would save Social Security, which again is the focus. Our focus was not to say, wait a minute, we are going to make every individual wealthy out of their personal accounts.

Our focus was, how can we get the job done to save Social Security with the least amount of money coming out of the general Treasury.

Mr. McCrery. And, you paid attention to the unified budget agreement as well?

Chairman Archer. Absolutely. And I am sorry that we don't have unified budget projections for all of the plans.

Mr. McCrery. Could you share with us the effect on the unified budget of your plan?

Chairman Archer. Right. But I can tell you that our plan increases the unified budget surplus over 75 years by $122 trillion. And that is what permits us to reduce the payroll tax by almost 4 percent.

Mr. McCrery. Thank you.

Mr. Crane. Mr. Stark.

Mr. Stark. Thank you, Mr. Chairman.

I keep trying to suggest, and I don't mean to damn you gentlemen with my faint praise——

Chairman ARCHER. Any praise will be most appreciated.

Mr. STARK. Well, there is really little difference. What I tried to show yesterday is that taking a chunk of money from the Treasury, whether we are in surplus or deficit, and transferring it to the trust fund is what mostly we are talking about, assuming you hold benefits. There were some plans, I understand, that cut benefits.

And so that the difference as I keep looking at it is that you would take this money and temporarily hold it in accounts which would be commercial securities, debt in equity.

And the current program, which is what I tried to mimic, would just invest it in government securities. I would take exception that under either plan there really isn't any personal savings increase. That technically is not correct because the accounts under your plan are not property of the individual, and to increase savings, it has got to be their property. It goes back to the government.

Plus, you offset those savings by reducing the purchase of government bonds, which also could increase savings. So I'm not sure that that is a selling point either way.

The biggest difference that I can see is that your plan anticipates the use of a higher return from equity. The 40 percent you put in bonds, I doubt if there is much difference, unless you are going to buy junk bonds. And I don't think that is what the investment advisors would do.

So it is the question of the 60 percent that you put in equity would yield a higher return to the Federal Government. And we compound now. Senator Gramm's idea of compounding was a wonderful discussion, but that is exactly what happens to the funds that are in the trust fund now. They are compounded, although they are invested in government bonds. That interest is still compounded. So there is nothing new there.

I just think we need to somehow start with what we are going to add. Where is the money going to come to add to—either to your accounts or to the Treasury as, or to the Social Security Trust Fund, as I would suggest. If it is going to come from the budget, then in 2027, you start running deficits. If, in fact, you are going to have a tax cut, as part of the Republican leadership plan, then you have got a deficit starting tomorrow, which I don't think any of us want, as would my plan.

And I guess I am just trying to suggest that as the first step in this executive session, when it comes, we ought to decide how much we are going to take from general revenues, regardless of where it goes, whether it goes into the stock market or whether it goes into these individual accounts. And we have to keep an eye on what other Committees are doing with that general revenue, I might add, because that surplus ain't all ours just to do with as we choose.

My friend Mr. McCrery says we don't have to worry about that but—so I guess my question is, wouldn't that be a good place to start as we view all of the plans is for us to decide how many dollars we have to take, basically in addition to the Social Security taxes, whether out of Federal revenue, let's presume, to shore it up?

Then step two is how are we going to invest it or what are we going to do with benefits, a whole host of other alternatives. Are we that close?

Chairman ARCHER. Well, we are certainly close to the extent that your plan and our plan both take identically the same amount of money out of the General Treasury over 75 years.

Mr. STARK. Pretty close, I think.

Chairman ARCHER. No, exactly.

Mr. STARK. OK.

Chairman ARCHER. Two percent of payroll you take out of the General Treasury, and 2 percent of payroll we take out of the General Treasury.

Now, in the way we budget, as you know, a big part of that is the unified budget surplus, the Social Security surplus, and so on. But I don't think we need to get into an arcane discussion about the budget overall.

But to compare the two, you and the Archer-Shaw plan take exactly the same amount.

The difference is though that you inject your money directly into the Social Security Trust Fund, which I have, as a traditionalist, I have trouble coming to grips with in mixing General Treasury funds with the Social Security Trust Funds. But perhaps that is not a big deal. But I just personally have always tried to stay away from that.

Second, the question of whether it is or is not their money. We provide specifically in our plan that it stays their money. It continues to remain their money straight on through their lives. And a consequence of that is, is that if they do die before they do reach retirement then they can pass that on to their heirs.

Certainly that is private-property right that establishes that it is their money.

But once they retire, and this is true—and a lot of my conservative right, which has come out against this plan, says, oh, but wait a minute, there is nothing to leave to their heirs after they retire.

But under the Chilean plan, which a lot of the conservative right, CATO, and so forth, really love, you are forced to convert to an annuity. Once you convert to an annuity, there is nothing to leave to anybody because it eliminates the risk of whether you live longer than life expectancy or shorter than life expectancy.

We say you have got to convert to an annuity. So I would say it is their money. You might quarrel with that. But irrespective of whether you believe that it is their money or not, the result of the savings aspect is there. Because what is the value of personal savings or private savings, which we are concerned about in this country? The value is not just having the money under the mattress. The value is that it is invested to produce jobs and increase productivity. And every dollar of this refundable tax credit is invested and put to work for the benefit of the entire country.

Mr. STARK. OK. Then let me just try this and I will—if the Chair will indulge me?

I get beat up, as many of us do at town meetings, about the notch, different retirement benefits. And it is conceivable that we have a lot of notches out there because of the value of the account

when people retire, which will inure to people who follow after us. But that is something not to think about.

I'm not asking you to accept this, but I would ask you this: If we then just said, take part of this—we both agree we about this 2 percent to save the plan—if we took a portion of that and invested it in the market in a lump sum and put it in and had it held by the trust fund and merely adjusted individual accounts so that everybody shared in the market ups and downs equally, could we accomplish the same benefit distribution that your plan does?

In other words, technically, wouldn't it be possible to almost get the same end result? Perhaps not the same feeling of independence and some of those things, but by holding the securities under one manager in one fund, like a mutual fund, say, for all the beneficiaries?

Chairman ARCHER. Well, I think you ask a very good question, and these are the kind of things that we are going to need to work through in executive session. I would say that if the government invests the trust funds that you run into the same problem that the President ran into with Alan Greenspan when he sat right at this same microphone, number one.

Mr. STARK. Have it done by a management company, like our C fund is doing.

Chairman ARCHER. Without trying to get in depth into that issue, but I, frankly, do not think that will pass the Congress. Eighty percent of the American people don't trust the Federal Government to invest the money.

Mr. STARK. I just was trying to see if I was assuming that we could get to the same benefit distribution and the same market benefit if we did it that way.

Chairman ARCHER. Yes. Sure. Sure. Economically you could.

Mr. STARK. All right.

Chairman ARCHER. However, I must point out that doesn't have anything to do with the notch problem. [Laughter.]

Mr. STARK. OK. Yes. If you could solve that, then put me on as a cosponsor, will you? [Laughter.]

Thank you, Mr. Chairman.

Mr. CRANE. Mr. Camp.

Mr. Ramstad.

Mr. RAMSTAD. Thank you, Mr. Chairman and Mr. Chairman and Mr. Shaw.

I certainly appreciate your leadership in this area and your advancement of this issue coming forward with this important plan. I enthusiastically support most of what you are doing. I certainly like, among other elements, the fact your plan guarantees a floor of current benefits with the potential for greater benefits.

Your plan will have a very positive, dramatic and immediate impact on some current beneficiaries, namely those people who in the system now between the ages of 62 and 70 who lose part or all of their current Social Security payments each year because they earn more than the law allows.

I have not had a town meeting in 9 years where Social Security beneficiaries haven't complained about the limit on earnings. Many of these people who are affected live in my district.

Can you please expand on how your proposal addresses the earnings limit?

Chairman ARCHER. It eliminates the earnings limit.

Mr. RAMSTAD. That is certainly the right answer.

Chairman ARCHER. At such time—if this program were adopted by the Committee today, it would eliminate the earnings limit. Seniors would no longer have to attempt to cope with that. Nor would the Social Security Administration. It is the single biggest administrative red tape issue in every Social Security office.

And we would gain immeasurably in the cost of administering Social Security, which is not figured at all into any of these estimates when we eliminate the earnings limit.

Mr. RAMSTAD. I really think that is a key element of your bill that needs to be highlighted. It is really an important part, as I said, of this legislation.

Let me ask a final question. As you can infer from my question of Mr. Stark yesterday, I am, like you, very interested in getting a bigger bang with our retirement bucks. And, unlike some of my colleagues, my constituents are not afraid of options which yield better rates of return with their hard-earned tax dollars.

How would your proposal, specifically the Social Security Guarantee Accounts, help workers get a better rate of return with their retirement dollars?

Could you just explain that for the record?

Mr. SHAW. That's from compounded interest and how that adds up. It is also the other factor of getting into investments that bring back more of a return than just the Treasury bills.

I think this is tremendously important. And when you look at all of the plans out there, with the exception of the Stark plan, every one of the plans turns to the private sector in order to increase the return. When you set forth that triangle box that Chairman Archer described, that is the only way you can get there. There is no other way to do it.

And I would say, and one of the speakers on the Democratic side mentioned the question of—in fact, I think it was Mr. Stark a few minutes ago—about how can you assume these things to be. We can assume it only by going back in 75 years of history. And these assumptions are made over the period of a couple of World Wars, other wars, the Great Depression. So I think as far as the estimate is concerned, if anything, it is overly conservative. I think the return will actually be more than we are projecting.

Mr. RAMSTAD. Well, thank you again, both of you, for your leadership in this critical area. There is no question in my judgment, the major issue facing this Congress and this country is the long-term solvency of Social Security. Certainly that is what my constituents are saying and I believe most Americans are saying.

And I hope that your approach, your legislation becomes the vehicle and we can, indeed, get something enacted into law to deal with this critical problem.

Thank you. Thank you, Mr. Chairman.

Mr. CRANE. Mr. Matsui.

Mr. MATSUI. I would like to thank you, Mr. Chairman, and obviously you, Mr. Shaw. You are really making a good-faith effort in trying to move the ball forward and deal with this problem. And

certainly the proposal is a credible proposal. I think I have said that a number of times.

One of the problems that I see in this entire debate at this time is the fact that when we first talked about doing Social Security first, we were more worried about protecting the Social Security surplus from the general budget. And now it appears to me we should be worried about using on-budget surpluses in terms of the Social Security.

I am starting to almost think that maybe we should try to deal with the budget first rather than Social Security because we may lift those caps or have a huge tax increase down the road. And if we do Social Security first, we might find ourselves really in a bind.

But we have already made that decision.

Here is what my concern is with respect to your proposal. And I kind of alluded to this yesterday, when we had both Mr. Stenholm and Mr. Kolbe appear before us. It is a fact—and I think Mr. Stark has really pointed this out—it is a fact that we are using significant general fund moneys. And let me must throw out a number. In 2034, you will increase the debt—this is absolutely astonishing when one thinks about it—by $11.7 trillion, $11.7 trillion.

And let me put this in perspective before you answer this. We are trying to deal with an issue today as if we were back in 1924 looking to 1999, a 75-year issue. Lindbergh hadn't even gone across the Atlantic Ocean, Babe Ruth hadn't hit 60 home runs then. And so we are trying to project from 1924 to 1999 essentially.

Look at all the changes that have occurred. And here we are trying to go from 1999 to 2074. And I know in your proposal, because you have said this a number of times, that you are going to have a $27 trillion surplus by the year 2074.

But, in 1924, if we would have made that kind of statement, people would have said, well maybe, maybe not. After all, we went through World War II, we went through a deep recession—depression, actually—and we went through a number of different major conflicts.

And so just in 34 years, 35 years, you are going to add to the debt $11.7 trillion. And bear in mind that under the projections we have by some of the actuaries that in 2034 we are actually going to have to start accumulating significant deficits in the on-budget.

And so we put your program in place, you know, which 35 years later, in 2074, we have huge surpluses, but in the meantime, we are going to have huge deficits and a huge debt.

And I just think the real danger we face here is the risk. And as we are trying to solve a 2 percent of payroll problem, which is actually 25 percent of the entire benefits, we may be creating a huge problem for our national economy, and certainly for our unified budget.

And I am not being critical because you are trying to do this in a responsible way, without cutting benefits and, obviously, without raising payroll taxes and trying to do this in a fashion that I understand, is consistent with where the President has gone on this.

But the reality is, we need to really discuss this with a little more seriousness. I really am sad that we lost the first 6 months of this year, spending all our time on the President's proposal. We

should have been talking about conceptual issues, about how we were going to really deal with this problem from a conceptual perspective.

And we are really running out of time right now. And all we have right now is your proposal and the President's proposal. We have Stenholm-Kolbe; we have a couple of others that are out there. But I don't think we have really had the time to think this through yet in terms of the impact of the overall national budget, the national economy and where we want to go.

And, again, as I said, I don't want to be critical of your particular plan because I think you are trying very earnestly to come up with the solution.

Chairman ARCHER. Bob, you ask a very, very important question. And it is one that I have asked all the way through. And we do need to look at the overall macro aspects that you have mentioned. The only thing that I would say to that is, we cannot look at it in a vacuum.

If we don't do anything, what will the debt be to pay the Social Security benefits?

In other words, it is compared to what? If you compare it to the President's plan, the President's plan has to increase the debt more than our plan does. Because the debt to the Social Security Trust Fund has the full faith and credit of the U.S. Government behind it, and it has got to be paid off the same as the public debt.

It is all part of the total debt responsibility. That is ultimately a levy on the taxpayers. And, I am not maligning the President's program, I am just making a comparison, that the debt ceiling has to go up more under his program than it does under our program.

Mr. MATSUI. If I may, Mr. Chairman. I think there is less risk at this time to the national economy in the President's program than perhaps in yours, and certainly Mr. Gramm's. At least in the first 15 years, the President actually reduces the national debt.

Chairman ARCHER. No he does not.

Mr. MATSUI. He does. I understand what you are saying in terms of the double accounting and all this, but he does actually reduce the national debt; whereas you put it out there in some kind of a quasithrift savings account, which, again, if all of a sudden those surpluses should disappear, at least the President hasn't put that money out there by way of tax cuts, which this basically is, or spending programs. You have got it out there in terms of a tax cut, essentially.

Chairman ARCHER. But, Bob, that just isn't—what you said is just not factually the case.

Mr. MATSUI. It is. It is.

Chairman ARCHER. Because if it were, his program would not require an increase in the debt ceiling. His program increases the debt of the country, does not reduce it, and requires an increase in the debt ceiling. And his own budget shows that. Our program actually increases the debt less than his does and requires an increase in the debt ceiling much farther down the line.

Mr. SHAW. Bob, the Archer-Shaw program reduces the total cost over 75 years of the Social Security—of Social Security by $100 trillion. And that is an actuarial figure, an actuary-proven figure.

And I would say one thing to you: There is no other way. Are you willing to decrease benefits? Are you willing to increase payroll taxes?

You can avoid what you just said by doing that, but you cannot avoid doing—you cannot avoid that unless you are willing to do those things.

I don't want to do that.

Mr. MATSUI. Do you deny what I just said in terms of the $11.7 trillion increase in the debt?

Mr. SHAW. No. I am not doing that. I am saying to you, over 75 years we save $100 trillion. We are legislating for the next generation.

Mr. MATSUI. No. What I am saying—Clay, what I am saying is you deny what I just said, that the $11.7 trillion will be added to the debt in the year 2034, 35 years from now, under your proposal.

Mr. SHAW. I am not either confirming it or denying it. You have figures in front of you. If you want to put your source in the record, you certainly can.

Mr. MATSUI. Well, you must have the numbers.

Mr. SHAW. I don't have those figures in front of me. There is a period——

Mr. MATSUI. I think it should be on the record by you. This is your proposal.

Mr. SHAW. Well, that is your claim that it is $11 trillion. And you can put your source in the record.

Mr. MATSUI. May I ask you this question then: What will the increase in the debt be in the year 2034 under your proposal?

Mr. SHAW. By the year what?

Mr. MATSUI. Pardon me?

Mr. SHAW. Which year?

Mr. MATSUI. Twenty thirty-four.

Mr. SHAW. It is about two and half trillion in 1999 dollars. It is about 11.7 trillion in the dollars out there.

Mr. MATSUI. No. No. No.

Chairman ARCHER. That's accurate, Bob, but you are looking at only a small segment of the entire picture. And you are only looking at it in a vacuum, not compared to all of the other possible answers to Social Security.

And it is only when you lay those side by side that you can make a decision as to which is the best way to go. I would prefer that any plan not in any way impact on the debt.

I would prefer that. But if we don't do anything, the numbers are staggering as to what will happen to the debt. And even under the President's plan, in the last 20 years, from 2055 to the year 2074, he has a shortfall of $76 trillion, which will be an increase in the national debt—$76 trillion.

The easier part is to get to 2055. The tough part is to get from there to 2074.

Mr. MATSUI. If I may just, and I understand my time has run out, but as the Ranking Member, if I could just seek a privilege—I appreciate this and I appreciate what you are doing. Here is what the problem is. You have a 75-year surplus, but in the first 67 years of the 75-year surplus, you accumulate massive debt.

And I understand what you are trying to do, but that is the reality of the situation. And I also, my last comment, think that this is much greater risk than what the President has suggested, even though his only goes 45, 55 years. It is a much greater risk.

Chairman ARCHER. But, Bob, to look at risk relative to debt, which is a valid way of looking at this, the debt to the Social Security Trust Funds is no less credible than the debt to the public.

Mr. MATSUI. I understand.

Chairman ARCHER. I don't think you would take that position. And I don't take that position. It has to be paid off. The debt service charges have to be paid off. They are all the same.

They are all included in the debt ceiling. And just to give you an example, because I don't have all the figures as they project out, but by the year 2009, the President's plan increases the debt under the debt ceiling, both public and government held, by $7.2 trillion. Our plan increases it by $6.6 trillion. So the risk under our plan on that analysis is less than under the President's.

Mr. MATSUI. My last observation is the fact that we do start running major deficits after——

Mr. SHAW. I think it is important to point out that under our plan all that debt is repaid, and then more, as you get into the out years.

That is how you can reduce the payroll taxes in 2050, and that is very important to realize. People really do not fully understand how this Trust Fund works. When you put money in it, you replace the money with Treasury bills, as you well know. And the money comes out the other side.

So you still have that money. You can run it through 10 or 12 times if you want to. The critical point that we have to concentrate on in this Committee in studying the various proposals, is 2014 because that is when the trust fund has to start cashing in the Treasury bills.

When the trust fund has to start cashing in the Treasury bills because there is not enough FICA tax in there to create a surplus or to even pay off the obligations of the trust fund, tax dollars have to come in and be injected in order to pay off those Treasury bills so that the Social Security Administration can fulfill it responsibilities.

So we can talk about 2035 as to when the trust fund goes broke, or we can talk about 2055 as to where the President pushes the drop-dead date on the trust fund. But under the President's plan as well as under existing law, tax dollars are going to have to come into play in the year 2014 in order to start retiring those Treasury bills to take care of the obligation because the FICA taxes are going to remain steady in the President's plan as well in the Archer-Shaw plan.

And that is what is going to create a negative cash flow. We need to keep our eye on the cash flow when you are talking about Social Security reform. That is paramount.

And when the Treasury bills are exhausted really is immaterial when you are talking about the cash that is going to be necessary to come in and bail out the fund to take care of its obligations.

That is, if you hold the line on existing benefits, and that is what we want to do. And you indicated by the shake of your head that

you are not willing to cut benefits and that you are not willing to increase payroll taxes. And I agree with you.

So I think we need to work together. And if there is going to be an alternative to this plan, we need to set that down as our basic premise.

Chairman ARCHER. I think, too, for the basis of this very important discussion, and I apologize for the time, but I think you are on to a part of things that we need to consider.

But it is important for all of us to understand that the numbers that we are looking at, that you referred to and that are put out by CBO are all based on the assumption that every surplus dollar will be used to pay down the debt.

Now, any one of these plans that uses surplus dollars to save Social Security is taken away from what CBO projects will be paying down the debt. Therefore, the debt will not really increase from where it is today, it will just increase from the baseline that CBO has assumed, which is not really a valid assumption because we know that all those dollars are not going to be used to pay down the debt.

We already spent $21 billion last year in the Omnibus Spending Bill; we spent another $7 billion this year in the supplemental bill. And there will be many, many other things that will come to pass. And that money will not be used to pay down the debt.

But if we are using the surplus that they assume will be used to pay down the debt in their baseline to save Social Security, of course the debt is going to go up.

Mr. MATSUI. Thank you, Mr. Chairman; I appreciate it.

Mr. CRANE. Folks, rather than proceed further at this time since we have multiple votes coming up on the floor, the Committee will stand in recess subject to the call of the Chair.

[Recess.]

Mr. CRANE. Will everyone please take seats, and in the interest of time, because we have a lot of further inquiries to be made of our distinguished witnesses, we will proceed. And the next person to be recognized is Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman. I really don't have any questions at this moment, but what I would like to say is that it was first referenced that there were no Members of the other party involved in the preliminary proposal that Chairman Archer and Mr. Shaw have brought forward, indicating that it was a Republican position. There are Members of the Subcommittee, of the Social Security Subcommittee who I know, speaking for one, was not involved in the drafting or the idea or concept that has been brought forth by Chairman Archer and Mr. Shaw.

And the idea that Chairman Archer has put forth this morning, the executive session of the Committee to discuss this proposal and other proposals and how we might incorporate different ideas to come up with a proposal that would be acceptable by both parties and the White House I think is an excellent idea and good opportunity for all of us to have input into solving this problem, this future problem in Social Security.

So I appreciate the opportunity and look forward to that opportunity. And I must say I am very honored to be on this Committee

and having served with some very fine people on this Committee on both sides of the aisle.

Thank you.

Chairman ARCHER. I thank the gentleman.

Mr. CRANE. Mr. English.

Mr. ENGLISH. Thank you, Mr. Chairman.

I want to congratulate these gentlemen on putting forward a proposal which I said at the time really set the standard for any other proposal in this debate. And I still feel that way.

I listened with great interest, Chairman Archer, to your exchange with Mr. Matsui, and I thought it was a useful exchange, but I think sometimes we get involved in arguments, particularly on fiscal policy, that seem to reach right through the heart of a question to seize upon the superficialities.

I think it is interesting how your proposal may affect the national debt, but I don't think you can consider that in isolation from how it also affects the national savings rate, which puts the debt into a level of significance.

Can you quantify for us how much your proposal is expected to impact on the national savings rate, and won't the transfers that go to those participants in individual accounts directly expand the national savings rate of this country?

Chairman ARCHER. Yes. I think that is an excellent question and very, very important. The national savings increases by $44 billion—and these are real dollars, inflation-adjusted dollars. We have been talking before about nominal dollars.

In real dollars, it increases by $44 billion over 10, $440 billion over 23, and $500 billion over 40, and $15 trillion over 75 years.

Mr. ENGLISH. These are changes of a scope that it is fair to say would actually dramatically increased our national growth rate.

Chairman ARCHER. I think there is no question. I think almost every economist would agree with that. When I have visited with Alan Greenspan, he has been very, very concerned about the savings rate. And he is very supportive of the fact that this will increase private savings and will be put to work and invested in jobs and productivity. And if we want to be able to have the answer ultimately in the next century to Social Security and to maintaining support for our elderly in general, whether it is Medicare or Social Security or any other form of support for our retired elderly, we have got to increase our savings now and we have got to increase productivity in the next century.

And when we put more invested dollars to work through these personal accounts, we have added tremendously to the initial savings and also to the productivity.

Mr. SHAW. Mr. English, as to the first part of your comment—just a few minutes ago before the break, Mr. Matsui and I were involved in a dialog regarding the $11.7 trillion of debt in 2034; it is important to know that that figure is correct, but it assumes that we start borrowing immediately even though we have a Social Security surplus for the next 15 years, which is not realistic.

And it is in nominal dollars only. It is about $2.5 trillion in 1999 dollars, and as a percent of the gross domestic product, it is much less than what the debt is today.

I do think it is very important that that information be added to the record. And since you brought the question of the debt up, I thought this was a good time to insert that in the record.

Mr. ENGLISH. I thank the gentleman.

One last quick question I would like to pose to both of you. You have offered a much broader range of investment options under your plan for participants in individual accounts than Mr. Kolbe and Mr. Stenholm have. Mr. Stenholm offered this as a virtue to his claim. Do you feel that it is important to offer, I believe under your plan, 55 different funds to potentially invest in? Or do you think a narrower range of investment options, as in the Kolbe-Stenholm plan, would be as effective, more effective, and perhaps have lower administrative costs?

Your comments?

Mr. SHAW. I will comment first. I think that the wide variety of investment houses would be very wise here because we are going to have wide-based investments. In other words, we are not going to have people putting all their money in one particular stock. Nor, philosophically, do we want the investment philosophy or method of just a few investment houses concerned here because it will have a dramatic effect upon those particular stocks that that investment house is watching.

We need to be sure that the investment house is qualified. In the Kolbe-Stenholm plan, or it may have been Senator Gramm's plan, he put forth the qualifications and how that particular investment house would be qualified by a sitting board composed of someone from the SEC, the Secretary of the Treasury, and several other people that he had in there.

It is important that they be qualified because we don't want every stockbroker in the country going off with these funds. So it is very important that we have qualified investment houses.

But I think we need to have quite a few of them.

Chairman ARCHER. Can I make one correction to my answer on the savings? The numbers that I gave you were the net national savings. The great concern today is the dearth of net private savings. And for net private savings, which is where we are at an all-time low in the history of this country, the increase would be $1.3 trillion over 10 years, $12.6 trillion over 30 years, and $138 trillion over 75 years.

Mr. ENGLISH. That is extraordinary. I thank you, gentlemen.

Mr. CRANE. Mr. Cardin.

Mr. CARDIN. Thank you, Mr. Chairman.

Well, let me first applaud both of my colleagues for coming forward with a plan that I think moves the debate forward, and I agree with you and hope that we will be able to come together with a plan to deal with Social Security in this Congress.

Let me just make an observation that I think there is a common thread through many of the proposals that we have heard both yesterday and, of course, the Archer-Shaw proposal.

Now if I could just quote from *Congress Daily* talking about Congressman Stark's plan, and it said, quote, "it is similar to the Archer-Shaw plan," end quote.

If others see these similarities, I think it is remarkable that we don't see a way to bring this together, and I hope that we will.

Mr. Chairman, I think that the Archer-Shaw proposal points out the power of market investments over time. As to what we can do by doing better on the return of the funds that we make available in one form or another for Social Security, the Stark proposal points out that there may be a more efficient way to do it. And I think that is worthy of our Committee's attention.

I applaud Mr. Stark for coming forward with that, with less risk to our commitment to reduce publicly held debt, which is also a goal that we would strive for.

Mr. Nadler pointed out that it is easy to modify the Clinton proposal to get the 75-year solvency if we are willing to use the market investment strategy similar to what is in the Archer-Shaw proposal.

And I applaud Kolbe-Stenholm and our U.S. Senators who were here for pointing out that we do need to have some real private savings accounts supplement Social Security, that the thrift savings model is one that could work within Social Security, that we need to be mindful of low-wage workers and their ability to accumulate some wealth or some better income security when they retire.

And that we do need to look at, what Chairman Archer you keep pointing out, and I agree, the low savings rates in this country.

Mr. Portman and I have worked on a bill that deals with private savings and retirement because I do think that is a key ingredient. Social Security was never meant to be the sole means of income security. And I do think as we look at dealing with Social Security that we need to be mindful of increasing the savings in this nation and particularly with the low-wage worker.

So let me just make an observation, if I might. First, I would hope that as we look for solution, I think there are three basic ingredients that come through many of the plans that have been suggested.

First is committing the surplus that has been generated through Social Security to dealing with the solution. The Archer-Shaw plan does that. Many of the other proposals that have been brought forward do that.

That we use market investment as a strategy to deal with the long-term solvency of Social Security, somewhere between 40 and 60 percent of the dollars that are available will bring us to that goal.

And that we include in the proposal real private accounts to supplement Social Security in a progressive manner for low-wage workers.

Mr. Chairman, I just want to make one more observation because I think it is key if we are going to be able to come together with the conclusion. And that is that our goal must be, get 120 Republicans and 110 Democrats who are willing to support the proposal.

I have a feeling that if we accomplish that, we are going to get a lot more votes on both sides of the aisle. But if we start off with the assumption that what have to get as Democrats consensus within the Democratic Party, or as Republicans within the Republican conference, that I am not so sure we will succeed.

And I would just urge us to be willing to work frankly and openly with each other to come to a proposal that will accomplish the goals that we have all spelled out.

And, Mr. Chairman, I think that you have offered a constructive proposal to lead us in that direction, and I would hope that we would follow through with your recommendations to have frank discussions to see whether we can't go the extra yard to reach the conclusion.

And I applaud you for your efforts.

Chairman ARCHER. Well, I thank the gentleman for his comments. You didn't ask for a response, but I am constrained to respond briefly. The gentleman has always been willing to pitch in and try to work on a bipartisan basis to solve problems facing the country, and I am greatly appreciative of that.

I would like to add, if I could, another couple of items that should be benchmarks for whatever the ultimate solution is. It should not leave cliffs at the end of whatever the number of years are that it presumes to save Social Security. That is truly unfair to the next generation.

I think we have got to have a system that once we have projected it, and I think 75 years is the right number, if not longer, but certainly under today's standards, that we don't then have a projection that it falls off the cliff at the end of 75 years.

If we were to do it only for 50 years, that it would not fall off of a cliff at the end of the 50 years. I think that is exceedingly important or we will not have done our job.

I also believe we need to be concerned about the unified budget surplus and what impact any of these programs has on the unified budget surplus because that is the basic macro barometer that we have always got to keep in mind.

And third, although it may not be necessary, I would hope that we could design a plan that would ultimately lighten the burden on the workers of this country by reducing the payroll tax while we accomplish our efforts.

That may not be essential to an ultimate bipartisan solution, but I think it is highly desirable.

I thank the gentleman for his comments.

Mr. CARDIN. Mr. Chairman, very briefly. Your first two points I agree with completely. I think it is extremely important that whatever recommendations we come out with, level the exposure on Social Security and not create the type of bar that we have seen that just presents problems in the future. I think it is a very good point, and I would concur with that.

Mr. CRANE. Mr. Portman.

Mr. PORTMAN. Thank you, Mr. Chairman.

And I would like, in the absence of his colleagues being here, to compliment Ben Cardin for, as the Chairman said, to be willing to pitch in and having a constructive role to play in the overall area of retirement savings on the pension bill, H.R. 1102, but also on Social Security.

I am able to say it, Ben, because many of your colleagues are not here to know how closely you work with us Republicans. [Laughter.]

Chairman ARCHER. That might hurt him. Who knows? [Laughter.]

Mr. PORTMAN. Also to commend Bill and Clay for the work you have done. As you know, I am very excited about this proposal. I think it is the basis for the final plan. I really do.

I go back to what Mr. Stark said, and this is really for his benefit. He is not here, but he talked about the similarities, and then said, really, the big difference, as I read what he said, was the, the efficiency issue, particularly focused on administrative costs, and that it is more efficient in essence just to take the general revenue Treasury surplus and put it right into Social Security.

I would make one comment on that and ask for your response to it at the end of my comment, which is that when you look at this proposal, the 5.35 percent is actually inclusive of administrative costs, and because of the pooling, which is unique to this proposal, the administrative costs are minimal.

In fact, what Social Security has said, as you know is that it will be 25 basis points, one quarter of 1 percent. I think that is a little high because of the pooling.

But as Charlie Stenholm said yesterday, Bob Kerrey said it in so many words, and Phil Gramm said it also, the administrative costs and the efficiency issue and all these questions depend on what kind of plan you have. And there are various ways to do this, but what you have done is come up with one where I think that issue is really resolved.

Second, I would say, in response to Mr. Stark, is that the similarities, although they are great, really are not quite as he described them, because where this plan is different is that instead of just taking those general revenues, you are actually getting not only the higher rate of return, and that is significant, it is about 2.35 percent higher, and, again, I think that is conservative, but also you are getting the power of the compound interest that you don't get with the Treasury investment.

And finally, the money is being put to work. Now that is more intangible, but when the Chairman talks about the personal savings rate, over a trillion dollars in 10 years and $55 billion in the national savings, those are SSA figures that relate directly to that putting money to work, which is a significance difference. It is a distinction with a major difference between those two approaches.

So I would say that this is, again, a plan I would think most Democrats should be able to embrace. And when you look at it intellectually, in concept it is similar in terms of its approach, but it has those benefits and it doesn't have the negatives that some of the other plans might have.

And I would ask if the Chairman, or the Chairmen, could respond to the administrative complexity side, and why you structured the proposal as you did.

Mr. SHAW. Regarding the administrative costs, the way the plan is structured once a year upon receipt of the earnings reports through the FICA process the Treasury will make checks payable to the investment houses as are involved in this.

Early on, when we were talking about individual retirement accounts, there was a great deal of criticism about, particularly, small accounts. But we have certainly done away with that criti-

cism because these will be qualified investors, which will receive the checks once a year. And so the administrative costs should be very, very little.

And also I think it is important to realize the administrative costs on the employer will almost be nonexistent.

Chairman ARCHER. Let me just add, too, the comment was made yesterday that the costs of the Federal Thrift Savings Plan, 10 basis points, I believe, was the comment, which I have been told in town meetings, well, tell me, what is 10 basis points, is that 10 percent?

No. That is 10 percent of 1 percent. And, because of the pooling and the aggregate dollars being so much larger than the Federal Thrift Savings Plan, certainly it should be no more than that, and in fact I have already inquired of a number of investment houses and have been told that it would be roughly 10 basis points.

Mr. PORTMAN. Well, that is exciting news too. And I think in the last 10 years we have seen remarkable strides on the private side, with our financial service institutions in getting those basis points down because it is very competitive out there. And there will be nothing more competitive than the trillions of dollars in Social Security to be invested in the economy.

And, again, the point is, the 5.35 percent is inclusive of those costs in any case. So you can really truly compare this to other proposals without worrying about the administrative costs.

I wish I had more time, I want to ask you more about the individual accounts, but again to just commend you both for moving the ball forward and I think, again, putting together a plan that is not only constructive to move the ball forward but actually can be the basis for a final compromise.

Mr. CRANE. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman and Mr. Chairman and Mr. Chairman. I want to thank each of you for your leadership on essentially what has been a logjam over the last few months as people have been waiting for the other guy to go first, and I want to commend you for your leadership.

I have been increasingly convinced that we should act this year, and that this fall I hope we can move something and get some legislation and move the process, hopefully, in bipartisan way. And clearly your leadership, I think, is heading us in that direction. And that is my hope.

I also want to build on Mr. Portman and Mr. Cardin's statement regarding increasing the opportunity for retirement savings. And perhaps, as we look at moving legislation similar to yours this fall, or later this year, we can also look at ways to combine with it some increased opportunities for retirement savings, giving people increased opportunity to contribute to their 401(k)s and their IRAs and address the need to create catch-up mechanisms, which will help working moms make up missed contributions while they are home with the kids before they return to the work force.

Some ideas that I hope we do look at. But the question that I want to address, you know, to Chairman Archer is, you know, yesterday Mr. Stark made a couple of strong statements regarding your proposal. And he used the term "phony" regarding individual

accounts. And I was wondering if you would address that point that he made.

Chairman ARCHER. Well, clearly, if you listen to the explanation of the accounts, they are anything but phony. They provide—it is provided under the law that they remain the private property of the individual. And because we have projections that Social Security will be saved forever, hopefully that will give some degree of certainty to younger people that there will be something there for them 50 years out or longer.

But, if worse came to worst, there would still be real wealth in their personal account that would be theirs. And that would always be there for them. And I think younger people could take heart that they are building wealth in these personal accounts. And as we mentioned, if they are unfortunate enough to die before retirement, then that is available to be left to their heirs. I don't call that phony.

Mr. WELLER. I remember the conversations I have had with senior citizens and conversations I have with college students, and I find the younger taxpayers and workers are, the less confidence they have in the current Social Security system. And I find the younger the worker is, the more interested they are in the personal account idea because they recognize that is one way that they can get something when it is their turn. And they find that idea very attractive.

In your proposal, you have—if someone were to pass on prior to making the decision to retire, you make the account part of someone's estate to pass on to their heirs. But then if they retired, it is no longer part of the estate. Can you explain your decision process and why you took that approach?

Chairman ARCHER. Yes, because it is a retirement account, pure and simple. And one of the concerns that a lot of people have is, having watched our progress with IRAs, that it will be invaded for other reasons, to buy a new home or for education or for a lot of other desirable purposes. That should never happen, cannot be permitted to happen with these accounts, because they are retirement accounts, solely.

And that means that in order to have the certainty of retirement, they must be converted into an annuity at the time of retirement. Now each individual selects the time when they want to retire. If they don't ever want to retire, and they don't want to be given the guarantee of the Social Security benefit, they can take that money and, at the time of their death, leave it to their heirs.

But once they retire, our plan does require that it be converted into an annuity with a fixed monthly benefit for the rest of their lives. Now that means they are not gambling on whether they will live less than average life expectancy or more than life expectancy. You give up those rights when you annuitize.

And, as a result, once you annuitize, there is nothing to leave to your heirs. And I would relate it again to the Chilean system, which a lot of right-wing conservatives believe is better than our plan. In Chile, you have to convert to an annuity when you retire. And there is nothing to leave to your heirs once you convert to an annuity.

If you took your IRA plan today and you converted it to an annuity so you knew you would have a fixed amount for the rest of your life, no matter how long you live, there is nothing to leave to your heirs.

But it is still your personal account. So when you get the benefit of knowing you are going to get a fixed amount for the rest of your life, you give up any option to be able to leave anything to your heirs.

Mr. WELLER. Quick follow-up on that: Do you have a minimum age when you can choose to retire?

Chairman ARCHER. Sixty-two because our focus, again, is to save Social Security. And we tried to make it as simple as possible without adding a lot of new bells and whistles and other things that many of the programs that we heard from yesterday do. We don't want to lose the focus. And the focus, being to save Social Security, does place 62 as the minimum retirement age as the Social Security system does.

Mr. SHAW. I think it is important, too, to add that there is a flexibility here. If somebody has a large retirement account and they choose not to retire, period, they don't have to. So just because somebody goes by these various age groups doesn't mean they have to annuitize because they do not. You can continue and hold the account until you die and then will it to somebody. And it is done estate tax-free. There is no tax involved in that particular transfer.

Chairman ARCHER. Yes, I tried to mention that earlier, but Clay described it a little bit better. But if you decide you do not want the guarantee of the Social Security benefit, you don't have to retire. Your money is yours until the time you die and you can leave it to your heirs.

But once you elect to retire and get the benefit of a guaranteed Social Security benefit, then you annuitize, and at that point, under any concept, private or public, you have nothing left to leave to your heirs.

Mr. WELLER. OK. Thank you. I see my time has expired.

Mr. CRANE. Mr. Hulshof.

Mr. HULSHOF. Thank you, Mr. Chairman.

Chairman Archer, you have, on a number of occasions, referenced the Greenspan Commission and your service. And over the weeks that we have been debating the future of Social Security and with all due respect to some of the proponents who were here yesterday, I think they have forgotten the lessons we have learned from the Greenspan Commission, and that is, as you recall and recounted for us, raising the payroll tax and cutting benefits is not the way for long-term solvency.

And I think, as someone mentioned, I think the American people are either with us or ahead of us when they recognize that the private sector, in witnessing the extraordinary success from the private sector, that we can bring this into this discussion. And so I also commend the two of you for stepping up to the plate.

I do have a couple of questions that are similar to what I posed to some of the witnesses yesterday.

Mr. Shaw, obviously, as the Chairman of the Social Security Subcommittee and being very active regarding Ticket to Work and the disability community in trying to move a bill that would help tear

down some of the disincentives for the disabled community, what, if anything, does your plan do regarding the disabled community because some of the plans yesterday affected it.

Chairman ARCHER. We leave the current disability program intact.

Mr. HULSHOF. OK, with no changes at all? Is that right.

Mr. HULSHOF. One of the things, too, that I asked Mr. Stenholm, the Archer-Shaw plan is mandatory in the sense that every worker who is paying into Social—who is paying into the Social Security system, would get the refundable tax credit that would go into the guaranteed account. What about these retirement plans such as, Chairman Archer, in your home state of Texas where groups choose to opt out or have chosen to opt out of Social Security. Would they be brought back in under the Archer-Shaw plan?

Chairman ARCHER. Only those people who have recorded payroll in excess of $5,000 a year, which is the minimum to qualify for Social Security today. In other words, the people who qualify are the ones who currently qualify under Social Security. And we don't change that.

Mr. HULSHOF. Yesterday, one of the Members of our Committee who presented himself as a witness, and I asked him pointed questions because I knew that you would be here today. And I attempted to get the gentleman from California to concede the point regarding worker choice that your plan proposes. He was very critical, and I couldn't get him to concede the point.

And so for the record, would you state what the Archer-Shaw plan does regarding the ability of the worker to make any direction or at least have any say as to how his or her payroll taxes or this guaranteed account could be directed.

Chairman ARCHER. Well, first, every single plan that sets up personal retirement accounts, everyone of them that you heard yesterday, will tell you first you can't simply invest this with your brother-in-law or anything you want to do with it. But if you want to invest it, it has got to comply with certain government standards and guidelines.

Now there are different ways to set that up, and that is a detail that can be worked out. But within those standards and guidelines set up by the government, the individual has complete freedom of choice as to which entity he or she wants to invest their money in.

A much broader range than the Federal Thrift Savings Plan has. Similar in nature, but a much broader range.

Mr. HULSHOF. Final question. Also yesterday, and I just ask you to comment, because regarding a response again a Member of the Committee who was a witness yesterday said something to the effect that high-income people could benefit greatly but that others would not. And I wanted to know what comment you might have in response to that allegation that was made at yesterday's hearing.

Chairman ARCHER. Well, first, let me say that one of the benefits of our program is, we protect the progressivity of the current system, which is very, very important. And we add to it because the refundable tax credit actually scores as giving 63 percent of the benefit to people under $50,000 a year of income. So we improve the progressivity, if you look at both together, which are part of the

solution to Social Security, we improve the progressivity of the current system.

That is number one. That is important to understand. And in so doing, we don't change in any way that progressivity, which would be required if you began to tinker with the bend points and this sort of thing, which is part of some of these plans that we heard from yesterday.

Now, obviously, people who are at a $50,000 to $70,000 annual income are going to get more into their account than someone who is making $20,000 a year because the 2 percent applies across the board. But according to the projections of the Social Security actuaries, and they picked the 5.3 percent annual return after administrative costs, as Congressman Portman said, they picked that number. We did not. They said that is a realistic number that we can have confidence in over 75 years.

Then no income worker in any category up to the wage limit will get enough money out of their account to exceed the promised Social Security benefit.

So it is not possible under their projections to justify the comment of some of the Minority on this. However, if you were able to see an average market return of 6½ percent, slightly over 1 percent more than what Social Security has projected, then some of the accounts would get above the Social Security benefit level. And those accounts would be toward the higher range.

Again, remember we are only, we are talking about people who aren't making in excess of $74,000. Now that is above average for American families, but that is not a rich category.

Mr. HULSHOF. Thank you.

Mr. CRANE. Mr. Tanner.

Mr. TANNER. Thank you, Mr. Chairman. I would like to ask at this point unanimous consent to submit a letter that Representative Kolbe and Stenholm have asked to insert in the record.

Mr. CRANE. Without objection, so ordered.

[The information follows:]

June 10, 1999

The Honorable Bill Archer
Chairman, House Ways and Means Committee
1100 Longworth
Washington, DC 20515

Dear Chairman Archer,

Thank you for the opportunity to testify before your committee yesterday. Again, we applaud the efforts of the committee to address the need for comprehensive Social Security reform.

During our testimony, you asked a very important question, "What is the impact of the Kolbe-Stenholm proposal on the unified budget surplus over 75 years?" While we do not have the exact figure at this time, we do know that our plan would increase the surplus more than the Archer-Shaw bill. We know this to be true for three reasons.

First, according to the Office of the Chief Actuary of the Social Security Administration, the Kolbe-Stenholm bill reduces the unfunded liability of the Social Security program by 52%, or $3.6 trillion. This is a more substantial reduction than under the Archer-Shaw bill. As such, the Kolbe-Stenholm plan reduces the general fund obligation to Social Security by a greater amount than the Archer Shaw plan. Obviously, the impact of a smaller general fund obligation under Kolbe-Stenholm implies a greater increase in the unified budget surplus vis-à-vis the Archer-Shaw plan.

Second, over the 75-year forecast horizon, the Kolbe-Stenholm plan reduces the effective cost rate of Social Security more than the Archer-Shaw plan. The average cost rate of the Social Security program under Kolbe-Stenholm is 14.0%, compared to 14.6% under Archer-Shaw. Again, smaller costs imply a greater reduction in the general fund liability, and hence a greater increase on the unified budget surplus compared to the Archer-Shaw plan.

Third, although both the Kolbe-Stenholm plan and the Archer-Shaw plan transfer general revenues to the Social Security program, the Kolbe-Stenholm plan contains a self-generating revenue source in the form of the CPI recapture. The Archer-Shaw bill does not. Consequently, the Kolbe-Stenholm bill requires less of already-projected revenues to be transferred, leaving a greater portion of these future projected surpluses untouched compared to the Archer-Shaw plan.

We hope you will share this information with the other Committee members during the continuation of the Committee's hearing today.

Sincerely,

Jim Kolbe Charlie Stenholm

cc: The Honorable Charles Rangel, Ranking Member, Committee on Ways and Means

Mr. TANNER. Thank you. I would like to thank Chairman Archer and Mr. Shaw for these 2 days. I think that it has been instructive and constructive. I believe that there is more public awareness now and really more general agreement about the nature of the problem and the fact that something has to be done.

And there has also been testimony and acknowledgements from all quarters that working together we can come together with some approach—savings rate, increasing the savings rate, wealth creation are constructive. They are all part of the equation, and your plan certainly is strong on that. Some of us have worried about increasing the Nation's debt with respect to how we fix this one prob-

lem. And it is part of the whole picture, as we have heard testified here before.

I believe that with further work and consultation, with the individual retirement accounts certainly being on the table and part of the solution, that you all have set the stage for something good to happen here. And I look forward to working with you to try to make something good happen.

Thank you.

Chairman ARCHER. I thank the gentleman, and I thank the gentleman for his continued interest, which has been ongoing for several years now in trying to realistically solve this problem and being willing to make tough decisions. And you stand apart from a lot of our colleagues in that regard.

Mr. CRANE. Mr. Lewis.

Mr. LEWIS of Kentucky. Mr. Chairman, I would like to thank you and Mr. Shaw for putting forward this plan. And you have already answered the question that I had that Mr. Hulshof asked about the retirement that are outside Social Security. But I guess the only problem and question that I would have now would be that this is such a straightforward, simple, commonsense plan that I wonder how it can possibly be passed. [Laughter.]

Thank you for your hard work and effort on this.

Chairman ARCHER. Thank you.

Mr. CRANE. Mr. Foley.

Mr. FOLEY. Well thank you very much, Mr. Chairman, and gentlemen for being here today. I was hoping Mr. Stark from California would be with us for this session because yesterday he took some detail and mentioned that the Shaw-Archer plan had phony accounting and was a ruse. And yet, when asked by Mr. Weller to describe the President's plan, he said I am not here to advocate the President's plan or to describe it.

So, I, as a Member, would like, if I could, to request Mr. Stark to give us an analysis, similar to the one he provided of yours, of the President' plan that he has laid before Congress, merely for comparison.

With that being said, and I am not certain if you have added your responses to that charge yesterday into the record, but I would like to do so today because I think you fairly adequately explain where he has raised some, if you will, phony allegations, ruses in your plan. And I think you have demonstrated clearly a very, very significant outline of your plan.

I think there are a number of things that America can look proudly at in your plan, and I think one of the things that I want to highlight, and Mr. Shaw brought it up earlier, first and foremost, the date that we would expect to start seeing excess going and out and coming into the system. And I believe you illuminated that to be 2014. Correct?

Mr. SHAW. Right.

Mr. FOLEY. The other thing I wanted to highlight, which you clearly do in your plan, is the effects on the national economy in the out years, the fact that you have not only increased national savings but you then allow the economy to share in that benefit, if you will, because people will be spending more.

The final thing, and if you would highlight that for me, and also, I think, what you illuminated, which was very, very significant, the fact that if you are finally capable after retirement to forgo that annuity, then you have, in essence, built up a lifelong opportunity for your children and grandchildren by transferring all those years you have made as payments.

Sometimes in this capital I find people talking about Social Security as if it is not the recipient's money, that it is manna from heaven.

So if you could kind of talk about both the effects on the national economy and, particularly, the impacts again, where you can take that asset and give it to your children, grandchildren, spouse?

Chairman ARCHER. I think you have adequately articulated it, and done very well. And I would appreciate it if you would enter in the record the explanation that responds to Mr. Stark's comment.

Mr. FOLEY. I will. And the other thing I want to make available, which I do not have today but will make available, there are some very, very significant editorials, if you will, in newspapers that represent the communities of both Mr. Shaw and myself, the Palm Beach Post Times and the Sun Sentinel, who have been glowing in their praise of your report.

Mr. SHAW. The Miami Herald.

Mr. FOLEY. And the Miami Herald. Those are three newspapers that we obviously at times come in conflict with based on editorial philosophy. But in this particular setting, when most people are afraid to talk about Social Security, the Post, the Miami Herald, and the Sun Sentinel have praised the initiative, have given what I think are glowing praise of both the word product and the ultimate outcome of what will occur.

And so I think that needs to be made a part of the record. Because it is not just Republicans or Democrats commenting on the Archer-Shaw plan, it are editorial writers who are looking for the seniors, particularly in my community, I am the seventh-oldest senior community in America out of 435 districts. So Social Security matters.

So I guess that wasn't a lot of questions. It was more for the record. But if Mr. Shaw wants to comment and if agrees to allow me to submit those editorials to the record.

Mr. SHAW. I think that would be very fine, and I am sure the Chairman will certainly be favorable toward inclusion of those editorials.

These are newspapers of very wide editorial opinions, it runs the full gamut, and I hesitate to try to describe any one of those editorial philosophies, but they are quite different from each other in the endorsement of candidates and the endorsement of ideas.

[The information follows:]

Palm Beach Post 5/5/99

Social Security plan beats a death warrant

Reps. Shaw and Archer would give everyone an IRA but put taxpayers, not mutual fund managers, in control.

The first Republican response to President Clinton's call to "save Social Security first" with the budget surplus is so obvious that you wonder why someone didn't think of it sooner. Someone like Mr. Clinton.

House Ways and Means Chairman Bill Archer, R-Texas, and Rep. Clay Shaw, R-Fort Lauderdale, who chairs the Social Security subcommittee, have come up with a proposal that diverges far from conventional wisdom. It will be a hard sell. Foes will drop a truckload of quibbles on it. But it makes sense.

Using part of projected surpluses, Reps. Archer and Shaw would give all who pay Social Security taxes a credit of 2 percent of their pay. The government would invest the money — coming from the Treasury, not from taxpayers — in mutual funds selected by the taxpayer. Social Security benefits and the employer's and employee's payroll tax would stay as they are.

At retirement, the contributor would get the Social Security benefit or the investment, whichever is larger. For most, that would be Social Security, although Rep. Shaw says young workers just entering the labor force might do better with their investment. If the contributor died, the investment pot would go to his or her heirs.

No one would pay higher taxes. No one would lose benefits. While the government would handle all the money, it could not decide how to invest it. Those are three of the four goals the planners set, Rep. Shaw says. The fourth is to solve Social Security's problems "for all time." The Social Security Administration actuary says the three goals solve the problem for the next 75 years — as far ahead as he can see — and that the plan might justify cuts in the Social Security tax starting about 2050.

The Archer-Shaw proposal would give everyone an individual retirement account, which is the bell that radical reformers keep ringing. But it wouldn't cost the individuals anything, which is an inducement that the radical reformers can't match. They want to kill Social Security and make people give the taxes they save to mutual fund managers. If the reformers are half-right, the GOP plan offers a better way.

The retirement accounts would make paying for old age a bigger part of the federal budget than it already is. But that was going to happen anyway, even in other reformers' plans.

The Archer-Shaw IRAs rely on surpluses. If deficits return, there will be problems. But the accounts use only one-third of surpluses the Congressional Budget Office projects will reach $2.7 trillion over 10 years. Congress would have to restrain its tax cuts and new programs.

It will be harder to explain to people why "their" retirement accounts, paid for with the surplus, add nothing to their Social Security benefits. The answer is that the accounts guarantee that they will get the benefits. That may not be good enough to sell the plan, but it's a basis for discussion.

4L THE HERALD, SUNDAY, MAY 2?, 1999
The Miami Herald

FIXING SOCIAL SECURITY

THE PRIVATE APPROACH

The Archer-Shaw plan offers security plus market growth.

Those who believe the country ought to fix Social Security this year should be heartened by the creative proposals of House Ways and Means Committee chairman Rep. Bill Archer of Texas and subcommittee chairman Rep. Clay Shaw of South Florida.

Their Social Security Guarantee Plan provides a Republican twist to similar proposals by President Clinton during his State of the Union Message.

The Archer-Shaw plan would tap projected budget surpluses to give wage-earners income-tax rebates equal to 2 percent of their wages covered by the Social Security payroll tax. The rebate would be credited to individual Social Security Guarantee Accounts to be invested in corporate bond and stock-index funds. Workers would select the fund from a government-certified list.

No benefits cut

At retirement, people would choose between an annuity based on their savings or the guaranteed Social Security benefit. Accounts could not be "cashed in." But, after the death of the owner, the balance — if any — would shift to survivors. It would pass tax-free to the estate of anyone dying before retirement.

The plan takes nothing from the existing Social Security plan. It cuts no benefit, imposes no new tax. What it does is channel some of the anticipated budget surpluses into Social Security, earmark the money for individuals and ensure that it is invested to increase returns to program. To work, tight caps must be imposed on commissions and management fees, and Congress will have give up tax cuts that deny government the needed revenue to maintain the program 15 years hence.

Naturally the plan is under attack. Republican conservatives are dismayed that it pulls the rug out from under "real reform," *i.e.* privatization. Democrats fear that it's a stalking horse for such privatization and some don't want "to lose" Social Security as a campaign issue.

Yet the case for ensuring that Social Security is fully funded for the next 75 years is simply made: As the post-World War II baby boomers retire, more people will be drawing benefits though fewer people will be paying into the program. The imbalance means money will run out about 2034. To fix Social Security now is cheaper and less painful.

The conservative bandwagon to privatize the system hits a number of sour notes: the enormous cost of maintaining benefits to current recipients, the inherent risks of stock markets, the inability to ensure adequate benefits for all, including housewives and the disabled.

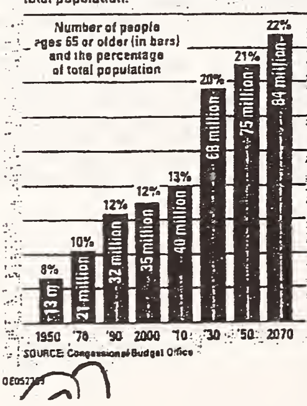
Some simpler fixes

There are simpler ways to fix Social Security — raising retirement ages and payroll taxes for example. But those haven't found much acceptance, and for ample reason. For example, it is unfair to African Americans to raise the retirement age when actuarial tables show whites born in 1998 are likely to outlive blacks by a decade.

The Archer-Shaw plan is doable, and Social Security actuaries say it would fix the program. Conventional wisdom in Washington has it that this is not the year. But when has there been a better year? The economy is healthy and government's coffers are full. Now more than ever, the country can afford to fix its social-insurance program. Let's get on with it.

U.S. POPULATION BY AGE

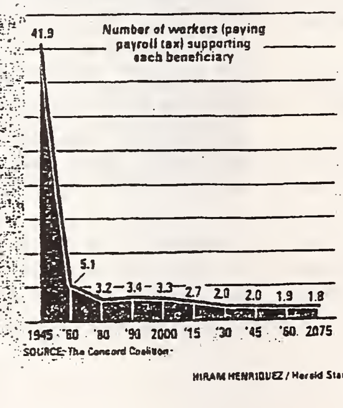
The number of people ages 65 or older is projected to increase dramatically by the year 2070, as well as their percentage of the total population.



SOURCE: Congressional Budget Office

WORKERS PER SOCIAL SECURITY BENEFICIARY

The number of workers supporting each beneficiary has dramatically declined since 1945, and is projected to continue to do so.



SOURCE: The Concord Coalition

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SOCIAL SECURITY

Shaw plan merits attention

U.S. Rep. E. Clay Shaw and colleagues from the Ways and Means Committee have come up with a Social Security plan that warrants bipartisan attention.

Independent numbers crunchers need to look at the specifics. If, in fact, "the math is there," as Shaw insists, the plan could serve as the basis for reform of the current, untenable Social Security system.

Shaw, a Fort Lauderdale Republican, chaired the subcommittee that drafted the plan, which makes use of current budget surpluses to bail out a retirement system that is headed for disaster because of the impending retirement of Baby Boomers.

Under the Shaw plan, Social Security payroll taxes could be used only to pay retirement benefits, and not for other government operations. Also, government budget surpluses would be used to finance 2 percent tax credits for wages up to $72,600 ($1,000 for a worker with a salary of $50,000). This money would be put directly into "Guarantee Accounts," which would be managed by individual workers, much as they currently manage 401(k) and other retirement plans.

Investments would be limited to 50 low-risk options divided between stocks and bonds. By harnessing the greater returns of private markets through the Guarantee Accounts, Shaw says Social Security benefits could be maintained at current levels.

By unveiling the plan, Shaw and Ways and Means Chairman Bill Archer took the sting out of President Bill Clinton's criticism last week that, "Republican leaders have yet to consider my proposals or advance any of their own."

Now, the GOP has a plan on the table, and Republicans can point out that among Clinton's proposals are private investment accounts not dissimilar to those in Shaw's plan.

Republicans also considered Clinton's idea for a trillion-dollar direct government investment in private financial markets, and then promptly and properly rejected it.

They, and a lot of Democrats, recognize that all that money in the hands of the government would create a temptation impossible for politicians to resist. Congress might try to create a system protected from government interference, but the system eventually would erode as politicians sought to use Social Security money for their own purposes.

The GOP has a plan on the table, and Republicans can point out that among Clinton's proposals are private investment accounts not dissimilar to those in Shaw's plan.

A defense contractor going broke? Then have the government use Social Security funds to shore it up. Don't like the way General Motors handled a strike? Then have the government unload GM stock. Object to a company providing benefits to live-in companions, and not just spouses? Then punish the company by having the government sell its shares, or worse, buy a controlling interest in the company and oust the leadership.

Rather than making buy and sell decisions on what is best for shareholders, decisions would be made on what is best for the politicians with the most clout.

Some Republicans in leadership positions are reluctant to take the lead in Social Security reform. They fear that with a presidential election just a year and a half away, advocacy of reform would hurt the GOP's chances of regaining the White House, and holding onto majorities in both houses of Congress.

They need to cast away their fears and take the offensive. Individual investment of Social Security funds in private markets is a good idea that has been proven effective and popular in Great Britain, Chile, Australia and other countries.

Direct government investment, on the other hand, is a dangerous scheme that would be hypocritical for the United States to adopt. How could U.S. officials, with straight faces, urge developing countries to divest their ownership in inefficient state industries when at the same time the U.S. government is buying up a sizable portion of the American economy?

In the marketplace of ideas, there's no comparison between Clinton's dangerous plan of massive government investment in private financial markets, and the alternative of individual investment.

Republican leaders shouldn't be afraid to go head-to-head with Clinton and Al Gore on this one, presidential politics notwithstanding.

And I think that simply shows that when you go and explain the common sense of what we are trying to do, that it is very understandable. And I think the newspapers all across this country should be looking for positions with regard to the Social Security disaster, pending disaster, that is out there.

They are quite correct. And we need to continue to look at that year 2014 because that is where the train wreck starts. And the entire train falls off of the track and into the river as you get further down the chain. But it would be a terrible, terrible mark on this Congress if we walk away from this thing.

Our grandchildren will curse us for it. We have the opportunity to do this, and to do it with a minimum amount of pain—actually no pain—to be able to commit some of the surplus Social Security dollars right now that are coming in to plan for the future, to front-load this.

And the solution that Chairman Archer and I have proposed saves it for all time. You know, we keep talking about the 75-year figure. That 75-year figure is only because that is as far as the Social Security Administration goes. But in reality, the Archer-Shaw plan solves Social Security for all time. In fact, it even solves it to the point that when you get into the later years, future Congresses will have the ability, if they choose, to reduce the employment tax.

And that is the toughest tax of all, particularly for the low-income people. That is a wonderful legacy for us to be leaving, instead of a pile of bills and a disaster for the payroll.

When you look at what is happening in Europe and other countries and the disaster that they have run into, we have the ability right now to solve the problem. That solution is in our hands.

I don't criticize anyone who has come forward with a plan. I think they are all well meaning. There are different philosophies involved. I think ours is the best, but some of the other people who have proposed plans believe that theirs is better.

But, in any event, I think we need to come together, and we need to be very careful not to criticize each other's plans but to really celebrate the fact that there are a variety of plans out there that we can look at.

Chairman Archer and I simply believe that the best way to go is without cutting benefits or increasing taxes in any way. We strongly believe that. And we will be in there pitching for our plan.

But I think both of us have an open mind for change, for any suggestions that the Minority party might have or any suggestions that may come forth from the Republican Party. There is not unanimity in the Republican Party on this, and we have seen some of the people who usually—these organizations that are on the conservative side—have taken some potshots at us. I think unfairly, but they are certainly entitled to do so. And they have carried with them, I am sure, some negative votes on the Republican side. Likewise, on the liberal side.

But I think what is going to happen here is, it is going to take the centrists in both parties to come forward and solve this thing and get this thing done and get it behind us. And we need to do it in this Congress.

I thank you for your comments, Mr. Foley.

Mr. CRANE. Well, I want to congratulate both of our witnesses on the outstanding presentation you have made today. And to just reinforce what you have said, that the solutions to this problem are not partisan I mean, it has nothing to do with Republicans saving Republicans or Democrats saving Democrats. It is trying to save the program in the interest of the American people, whether they are registered voters or not even voters.

And in that sense, I think you have done an outstanding job, and you both deserve enormous commendation. And with that, I will let you two, as witnesses now, come back up here on the panel and resume your Chairman titles.

Chairman ARCHER. Mr. Chairman, before we do that, may I just briefly close by saying something that I intended to say earlier and failed to do?

Mr. CRANE. Yes, indeed.

Chairman ARCHER. The President of the United States deserves to be complimented for making us focus on this issue and with the concept of saving Social Security now as being predominant. And we should not be so partisan that we do not recognize that he has made a contribution to this effort in that regard.

I believe also that we should never lose the focus as we go through this deliberation, and that focus should be to save Social Security. Many see this as an open door to add all kinds of new things and new concepts and, oh, we do these wonderful things. But every time you do it, you lose something. And we should focus entirely on saving Social Security in the best possible way. And I believe that is what we have done. And I hope that we can proceed from this model on a bipartisan basis to see a resolution signed into law.

And I thank the Chairman.

Mr. CRANE. Well, I think we can anticipate that, and Jack Valenti reassured that his next movie is "Saving Social Security." And you are the featured stars. [Laughter.]

I now would like to invite our next witness to come to the dais, Steven Goss, Deputy Chief Actuary, Office of the Chief Actuary, Social Security Administration.

Chairman ARCHER [presiding]. Mr. Goss, welcome. I have already publicly complimented you, and I do so again. You and your staff have done outstanding work to help us along in this process.

And contrary to what many Members would like to assert, including myself, by the way, that we know better than the estimators and that they are really wrong and they haven't considered this and they haven't considered that. And I have criticized frequently over the years the estimates of the Joint Committee on certain tax proposals.

The reality is, we must accept one standard on which we act, irrespective of what our own subjective discretion might tell us. And for the purposes of Social Security, you are that standard. And any plan that is adopted must meet your standard. And Members might want to argue with it, but we should establish early on that that is the barometer that all of us must comply with.

So, I welcome you today and thank you again. And we will be pleased to hear any testimony that you would like to give us.

STATEMENT OF STEPHEN C. GOSS, DEPUTY CHIEF ACTUARY, OFFICE OF THE CHIEF ACTUARY, SOCIAL SECURITY ADMINISTRATION

Mr. GOSS. Thank you very much, Mr. Chairman and Members of the Committee. It is truly a pleasure to be here today, especially following, Chairman Archer. It is truly an honor.

I have some prepared written comments to be submitted to the record—I would just like to make a couple of brief comments.

Chairman ARCHER. Without objection, your entire written statement will be included in the record.

Mr. GOSS. Thank you. I am here today to discuss with you the nature of the estimates that we make for the status of the Social Security Program on a financial basis and for proposals, especially the proposals that you have been discussing for the last day and a half.

The Social Security Act requires that there be submitted, the Trustees of the Social Security system submit an annual report to the Congress providing estimates of the financial operations of the program over the next 5 fiscal years as well as provision of the actuarial status of the program.

This actuarial status has been determined over the years to be interpreted as an assessment of what the financing of the system appears to be over the next 75-year period, something that has been discussed to a fair extent already today.

Our purpose at the Office of the Actuary of the Social Security Administration is to try to provide the most objective possible analysis we can for the present-law system as well as the legislative proposals that are put forth by Members of the Congress, as well as the administration.

I appreciate very much your comments, Chairman Archer, of appreciation. We are doing our best, and hopefully this will play some small role in providing the information that policymakers like all of you need in order to come up with a very good solution for Social Security for the future.

The current status of the Social Security system, as you know, leaves us with 44 million beneficiaries currently receiving benefits that are provided by about 150 million current workers paying taxes into the system.

As already mentioned, there are generally three dates that people focus on. Under the current-law financing of the system and under the current intermediate assumptions of the Social Security Trustees' Report, the first date is, of course, 2014, at which time taxes coming into the system will first become insufficient to pay for the annual cost of the system.

The second date is the year 2022, the year in which the trust fund dollar amount will reach a peak and will begin to go back down; you might refer to that as the year in which taxes plus interest on the trust fund become insufficient to pay for the current cost.

And the third date is the year 2034, the year in which even with access to the moneys in the Social Security Trust Fund and the ability to redeem those bonds, Social Security will not have sufficient money to pay benefits on a timely basis.

You should keep in mind, of course, by way of getting a sense of the magnitude of the financial situation of Social Security as of 2034, that the tax revenue coming into the system will represent about 71 percent of the cost of the system under present law.

The measures of the system that have been developed over many, many decades are currently represented in the Trustees' Report. First and foremost, and certainly most basic, in terms of looking at the ability to pay these benefits over a 75-year period is whether or not the Social Security Trust Funds will become exhausted. Taxes are insufficient coming into the system and there is not a trust fund to draw upon, because without borrowing authority, Social Security would not be able to pay full benefits on a timely basis.

So the first and foremost measure certainly is the exhaustion of the trust fund. But the most widely and commonly looked at measure for the system is the so-called actuarial balance or the actuarial deficit, as has been discussed earlier today, which is estimated at 2.07 percent of the taxable payroll (the expected taxable earnings) over the next 75 years.

One can interpret that as requiring a tax-rate increase of 2.07 percent, or any other change that would have equivalent value, in order to make benefits payable over the next 75 years.

A third measure which has come into more interest and more importance I think in very recent years, starting with the 1994–1996 Advisory Council on Social Security, has been a matter of looking not just at the ability of the trust funds to pay benefits in full over the full 75-year period, but also looking at what the financial status of the system is at the end of that period.

The best measure we have been able to come up with, for portraying this, is the stability of the trust fund ratio; that is, whether or not the trust funds are growing at about the same rate as the outgo of the system. And when that test is met, as Chairman Archer has mentioned and Chairman Shaw also, then we are in a situation where the system will be not only solvent over the 75-year period but will be in such a position for the indefinite future.

You have been discussing 10 different plans over this past day and a half. We have done actuarial estimates for all of those plans, and all of them have been found through the intermediate assumptions of the 1999 Trustees' Report to meet solvency over the 75-year period. Although all of them do meet the solvency criteria as laid out, these plans differ in many, many ways as you all well know.

And I am very happy to be here today and will be extremely happy to attempt to answer any questions you have.

Thank you.

[The prepared statement follows:]

Statement of Stephen C. Goss, Deputy Chief Actuary, Office of the Chief Actuary, Social Security Administration

Mr. Chairman and Members of the Committee, thank you for the opportunity to describe the work of the Office of the Chief Actuary in assessing the plans to reform Social Security that have been developed by Members of Congress.

The Social Security Act requires that the Board of Trustees report annually to the Congress providing the expected operations and status of the Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI) Trust Funds for the next 5 fiscal years and "a statement of the actuarial status of the Trust Funds." The Office of

the Chief Actuary works with the trustees in the development of this annual report of the financial status of the program under present law.

In addition, the Office of the Chief Actuary provides to the Administration and to the Congress estimates of the financial effects on the Social Security (OASDI) program of potential or proposed legislation. The mission of the Office of the Chief Actuary is to provide objective analyses that will permit policymakers to make informed decisions about the future of the Social Security program.

Current Financial Status of The Social Security Program

The Social Security program currently provides monthly benefits to more than 44 million individuals. The primary source of financing is a payroll tax on the nearly 150 million workers in covered employment. Tax revenue currently exceeds the cost of the program, so the trust funds are growing. Trust funds are currently almost twice the size of the annual cost of the program, and growing.

Based on the intermediate assumptions of the 1999 Trustees Report, tax income to the OASDI program is expected to exceed cost until 2014. The combined OASI and DI trust funds are expected to continue growing until 2022. The combined trust funds are then expected to decline until they are exhausted in 2034.

At the point of trust fund exhaustion in 2034, continuing tax income is expected to be equal to 71 percent of the cost of the program.

Measures for Evaluating the Long-Range Actuarial Status of Social Security

The Social Security program is a complex system developed more than 6 decades ago to provide monthly benefits that offer what has been referred to as a "floor of protection" against loss of income due to retirement, death, or disability. The program provides a blend between individual equity and social adequacy that has evolved through the judgement of several generations of policymakers.

Both Annual Trustees Reports and estimates by the Office of the Chief Actuary for legislative proposals focus primarily on the financial status of the OASDI program. Because current program financing is expected to be adequate for the full payment of benefits on a timely basis for over 30 years, I will describe the criteria used for evaluating the "actuarial status" of Social Security over the long run.

The actuarial status of the OASDI program is evaluated over a 75-year, long-range projection period. This period provides a view of the adequacy of financing over the entire lifetime of virtually all current participants in the program, from the oldest beneficiaries to the youngest workers. This period also provides the opportunity to view the full, mature financial effects of legislative proposals that may take decades to become fully implemented.

The most fundamental criterion for evaluating the financial status of the OASDI program is its ability to pay full benefits in a timely manner. The inability to do so is indicated by expected exhaustion of the trust funds within the 75-year period.

Perhaps the most commonly used measure of long-range solvency of the OASDI program is the actuarial balance. This measure indicates the size of the difference between expected financing and cost for the program over the 75-year period, on a summarized present-value basis. An actuarial balance of zero indicates that financing over the 75-year period is equal to the expected cost of the program, with enough left over for a trust fund balance at the end of the period equal to the annual cost of the program.

The actuarial balance is expressed as a percentage of taxable payroll over the 75-year period. Under the intermediate assumptions of the 1999 Trustees report, the estimated actuarial balance is −2.07 percent of taxable payroll. Because this balance is negative, it is referred to as an actuarial deficit.

An additional important measure for evaluating the actuarial status of Social Security is the stability of the financing at the end of the 75-year period. Financial stability is achieved at the end of the period if total program income is sufficiently meets the costs of the program and maintains stable trust fund reserves. Stability of trust fund reserves means that the trust fund balance expressed as a percentage of the annual cost of the program (the "trust fund ratio") is essentially constant.

At the request of the Chairman and other Members of Congress, the Office of the Chief Actuary has assessed a number of plans to reform Social Security. While many of the plans would bring the Social Security program into long-range actuarial balance, the plans are all different to some degree. The Office of the Chief Actuary will continue to work with the Administration and the Congress as policymakers develop and consider these, and any additional plans, for addressing the long-range financing issues facing the Social Security program.

I will be happy to answer any questions.

Chairman ARCHER. Thank you, Mr. Goss, and I will inquire for a few minutes. I apologize that I have got a meeting at 1 o'clock and I will have to leave, and thereafter Mr. Shaw will preside.

There has been a lot of discussion about why 75 years, and some Members of the Committee have made light of it and said, well, let us talk about 150, or why don't we talk about 200, or maybe only 50 is enough.

Since you have been working with this, and you have the responsibility, what is the relevance of using 75 years as a benchmark for Social Security's long-term solvency?

Mr. GOSS. The 75-year period is a number that I believe was introduced into the Trustees' Report around 1972 as the defined long-range period. The fairly well-known rationales for seeing this as a very appropriate period are, first of all, this is a period that is long enough to generally encompass the remaining lifetime of all current participants of the program, that is, people not only receiving benefits, but people who have already contributed to the program.

If you take for example some of our youngest contributors in their late teens or age 20; most of those people can expect to live to no longer than about age 95, which would be 75 years from today.

So, first of all, the 75-year period is long enough to encompass the remaining lifetime for virtually all of the current participants in the system.

Another reason why we believe the 75-year period is a very important period to look at, is that when considering not only the effects of past legislation, but also the effects of legislation that we are looking at today and we will be looking at in the near future, much of this legislation takes a number of decades to evolve and to mature and to have its full effect on the system.

One remark I would make about looking beyond the 75-year period is that there have been estimates made in the past going into perpetuity. Many of the measures we look at under Social Security, like the actuarial balance if looking into perpetuity, would begin to have far less meaning for a technical reason. This is because the cost of the program rises at very nearly the same rate as the discount rate which is the interest rate on the Trust Fund Special Issue bonds.

As a result, if we were to do an actuarial balance calculation into perpetuity, we would essentially get a measure of what the balance looks like at about the 75th year alone. And it would not be a measure that would effectively reflect what is happening over the course of the next 75 years.

The only other point that I would make is that many people have remarked that they think 75 years is an extremely long period of time to look at because of the uncertainty. I think part of the reason for a compromise of staying at 75 years is that to go farther becomes even more uncertain in terms of our ability to really see with any clarity what will happen in the future; whereas, to look at a shorter period of time would not leave us in a position to see

the remaining lifetime of current participants and to be able to fully see what the effects of the proposals would be.

Chairman ARCHER. But 75 years has been the standard as to whether Social Security is solvent. That has been used since 1972.

Mr. GOSS. That's correct.

Chairman ARCHER. I remember serving on the commission in 1982, and we were charged with meeting a 75-year responsibility in 1982. And as I have mentioned before, one of the reasons that I opposed the ultimate suggested solution, one of the reasons was because I didn't think it saved the program for 75 years.

And as I have mentioned before, sadly enough, I was correct. But I hope we can do a better job when we adopt our solution this time.

I have one other question, and then I am going to yield the Chair to Congressman Shaw.

During yesterday's hearing, one of the witnesses kept referring to private market investment. I don't mean a Member of the Committee, but one of the witnesses kept referring to private market investment as, quote, "gambling with Social Security," unquote.

Is it reasonable to expect that private market assets will continue to yield higher rates of return than Treasury bonds over a long-term investment horizons? And are you aware of any model or any economist or any actuary that projects differently?

Mr. GOSS. I am not aware of anybody who would contest the suggestion that returns on private securities, especially stocks, will, on average, in the future exceed the rate of yield that one should expect on government bonds.

I think the appropriate remark that people do make is that, as in the past, the year-to-year variability in the returns that one might expect from the stock market will almost certainly be greater than for bonds. But the expectation that the yield on stocks will exceed the yield on bonds over long periods of time I think is not contested.

Chairman ARCHER. Well we, unfortunately, as a democracy normally look at a long-term problem as that which lies between now and the next election, but for Social Security, it is essential that we project long term.

And you have explained why we need to look at 75 years. And when you do project long term, then you have to look at returns, although they might fluctuate in the short term in the way of averages because it is truly a long-term program.

And I thank you for your comments. Again I thank you for your good work. And I apologize that I am going to have to leave.

But it is important that Members ask probing questions and get your responses on the record so that that will be available for analysis as we move forward with our effort to solve this on a bipartisan basis.

And, again, I thank you.

Mr. Shaw, will you preside?

Mr. SHAW [presiding]. Mr. Houghton.

Mr. HOUGHTON. I would like to ask a question. I am looking at table 1, and if I understand it, that the income rate starts getting below cost in the year 2015 and then continues to 2030. And then the income rate increases, starts increasing, and then it gets over cost in the year 2044.

There is a 5-year period there when the income is over cost, and then from the year 2050 it goes below. Maybe you can explain that to me. And it continues ad infinitum, the cost of over-income for the rest of the period.

Mr. GOSS. Thank you very much, Representative Houghton. Yes, I think I can do that.

When you are referring to table 1, you are referring to table 1 in the memorandum that we did, I believe, for Representatives Archer and Shaw's plan.

Mr. HOUGHTON. Yes.

Mr. GOSS. The column that you are talking about, this annual balance, represents in effect what the difference between tax income and benefit outgo is under the Social Security system.

Mr. HOUGHTON. Right.

Mr. GOSS. Included in this column also is another item which is the amount of money that would be transferred back to Social Security as proceeds from the Social Security Guarantee accounts. And that is actually included in the far left column, which is referred to as cost rate, and it is the reason why the cost rate shows up lower than under present law.

Now, the specific point that you make about the fact that in the year 2044 our tax income reaches the point where it is exceeding the net cost of Social Security for that period and then it drops in the year 2050 is due to the fact that the specification of the proposal is that as of 2050 the FICA payroll tax rate would be reduced by 2.5 percentage points.

Mr. HOUGHTON. And then another one in 2060?

Mr. GOSS. And then another one in 2060. If the FICA tax rate were retained at the full 12.4 percent, then the positive values you see for the annual balance, the cash-flow positives, would continue on into the indefinite future.

Mr. HOUGHTON. But help me on the numbers. If it is going the wrong way, because you have had a price cut or a cost cut as far as the FICA taxes, doesn't that ultimately catch up with you, or is the offset from the trust fund reserves so great that it makes up the difference?

Mr. GOSS. That is exactly correct. What is happening is that, as you will see in the next column over showing the trust fund ratio, as has been discussed here so far today, there is a desire to keep the level of the trust fund growing generally at about the same rate as the rate of growth of cost of the system.

Because the cost of the system is growing at a rate that is in fact slower than the yield or the interest rate on trust fund assets, in order to maintain the trust funds growing no faster than the cost of the program, it is in fact necessary, to utilize some of that interest that the trust funds are yielding in order to pay the benefits for the program.

If, for example, we were to maintain this annual balance column at zero or higher, then our Trust Funds would simply be growing very rapidly in the future because all of the interest earnings in the trust funds would be retained within the trust funds and they would continue to compound.

Mr. HOUGHTON. And so in fact that in the year 2050 and in the year 2060 we have an insurance policy. You don't have to reduce those, the FICA taxes?

Mr. GOSS. The plan would not have to reduce those FICA taxes as of the year 2050 and 2060. You are correct.

If it did not, then the amount of bonds in the Social Security Trust Funds would be growing very, very rapidly at that point under current assumptions.

Mr. HOUGHTON. OK. Now let me just ask you one other more general question. You know, we have heard all the details, and we have been going around these things for a day and a half now. What is the big risk?

Mr. GOSS. The big risk? Under what plan?

Mr. HOUGHTON. This.

Mr. GOSS. Under this plan?

Let's see, when we talk about risk, I think what you are probably referring to is the notion that any of the plans, in fact—I think it has been stated that 9 out of the 10 plans you have been considering for the last two days—introduce something really that is new to Social Security. This is the notion of having advance funding with a portion of that advance funding invested into the equity market, into stock.

We do know clearly that stocks are more variable in their return and maybe somewhat less certain in terms of what their average return will be in the future as compared with some of the other assumptions that are made by the trustees for the Trustees' Reports.

I think it is probably——

Mr. HOUGHTON. Are you saying that the biggest risk is the fluctuation in the market?

Mr. GOSS. I would suggest that the biggest risk, given this proposal put forth as legislation, to failing to meet Social Security solvency, would be a failure of the markets to achieve the yields that had been assumed on an expected basis over the next 75 years.

As you have seen in this memo, we did do a sensitivity analysis, which suggested that if the market yields are lower by a full percentage point, then the result would not be as favorable as of course we would expect.

Mr. HOUGHTON. Well, I would submit, and if I could just take a minute longer, Mr. Chairman——

Mr. SHAW. Go ahead.

Mr. HOUGHTON. I would submit that the biggest risk is not that. I would say the biggest risk is that we continue or accelerate our spending as a government to the point where we are unable to borrow the type of money which is going to be needed in the interim. And so the important thing to me is that we recognize these numbers and recognize that we are going to be taking a big gamble here in the interim years. But it comes out all right if we don't exaggerate our spending in other areas.

Mr. GOSS. Very good point.

Mr. HOUGHTON. Thank you very much.

Mr. SHAW. Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman.

Mr. Goss, in looking at the Gramm plan and comparing it to the Archer-Shaw plan, I would like to know from an actuarial stand-

point and if you feel qualified to speak from a budgetary standpoint, what is the difference between carving out 3 percent from payroll taxes, as the Gramm proposes, and simply infusing 2 percent from general revenues into private accounts?

What is the difference between those approaches in terms of the Federal budget, the unitary budget surplus? Is there an advantage of one over the other in the short term in so far as accumulation of national debt is concerned? Can you address that?

Mr. GOSS. First of all, Mr. McCrery, let me suggest that on the Gramm plan, as we understand it, and we have developed estimates for it, the plan would not be what we might refer to as a "carve-out," initially at least. The contributions, which start out actually at above 3 percent of taxable payroll, more on the order of 4 percent in the very early years, dropping down eventually to 3 percent, would be initially paid for from the general fund.

And I believe the mechanism is that the money would be provided from the trust funds but with reimbursement from the general fund of the Treasury.

So the net cost, in fact, is borne out of the general fund. Under Senator Gramm's plan, however, as seen in our memo, there is a point in time at which the transfers back from the individual accounts to the Social Security system result, much as with Chairman Archer and Shaw's plan, in a point where the cost to the system is being more than met by current taxes plus the amount of money being transferred back from the individual accounts.

And similar to the Archer-Shaw plan, Senator Gramm has suggested, although I don't know if he has actually locked this in, that one thing that could be done with the excess tax rate situation we have is that we could redirect a portion of the Social Security 12.4 percent FICA tax rate to cover the cost of the contributions to the individual accounts. In effect, starting as early as the year 2000, a portion of the individual accounts contributions would be covered from Social Security FICA taxes.

And, in fact, there are the intermediate assumptions of the Trustees' Report where it would be possible, I believe in the year 2040, to have the entire 3 percent covered from what we might refer to as a "carve-out" from the Social Security system.

Mr. MCCRERY. What year was that?

Mr. GOSS. The year 2040. And in 2040 we would reach a point where the cost of the Social Security system would be such that the FICA tax that is directed to the OASDI Trust Funds could be reduced by 3 percentage points below the 12.4 percent level, which would mean that, at that time, that 3.0 percentage points of the FICA tax rate, if still in effect, could be redirected to handle the cost of the individual account contribution.

The alternative, of course, is that the 3.0 percent could be used to lower the FICA tax rate, in which case the entire burden of paying for the individual contributions would remain on the general fund.

Mr. MCCRERY. So, are you saying that there is essentially no difference in terms of the macroeconomic effect of the two approaches, at least between now and 2010 or 2020?

Mr. GOSS. I think in comparing these plans, I would agree with you, they appear to be fairly similar in that regard. The one dif-

ference is more quantitative than qualitative and that is that the Gramm plan has somewhat higher contributions starting out a little over 4 percent equivalent of payroll, relative to the 2 percent under the Archer-Shaw plan. It eventually goes down to 3 percent. But I think that would be the primary difference initially.

Mr. McCRERY. In your calculations, have you taken into account—well, let me stick with the Gramm plan. Real quickly, I understand that for purposes of your calculations, you assumed 100 percent participation in the voluntary private accounts. Is that correct?

Mr. GOSS. That is correct.

Mr. McCRERY. Why did you make that assumption?

Mr. GOSS. In the case of the Gramm plan, as we understood it, and I am hoping our understanding is still current, the nature of the plan was such that, for people who were participating in the plan and having one of the individual accounts put forth, these people would be guaranteed to present-law Social Security benefits plus 20 percent of whatever the proceeds might be under the individual account that would be developed.

Therefore, presumably, the worst that a person could do is, if they somehow managed to lose the entirety of the value of their individual account, they would still be guaranteed to get present-law Social Security benefits.

But if they retained the value of the contributions that went into their individual account and had them increase to any extent, they would receive, in addition to Social Security benefits, an amount equal to at least 20 percent.

So in that situation, we would find it difficult to believe that many people would turn down the option.

Mr. McCRERY. Well, would you make any calculations based on a lower rate of participation?

Mr. GOSS. We didn't. Of course, the extreme case would be if no one chose to participate, in which case we would be precisely where we are today with present law. And there would be no improvement in the actuarial status of the program at all.

In all likelihood, if we were to assume partial participation, we would move somewhere in between the solvency that is indicated under the Gramm plan and the situation that we have currently under present law, where we do not have sufficient funds to pay for the full 75 years.

Even with participation that is somewhat less than 100 percent, I believe because of the nature of the extent of the solvency created under the Gramm plan, even if we had 80 or 90 percent, we would very, very likely still be in a situation where the long-term projection would be the Social Security system would be solvent under the Gramm plan.

Mr. McCRERY. If I may, just one more question. With respect to the COLA, I know that some of the plans you analyzed have explicit reductions in the COLA, but for those plans that do not contain an explicit legislatively derived reduction in the COLA, did you assume in your calculations any reduction in the cost-of-living adjustment?

Mr. GOSS. No, we did not. I should mention, though, that the 1999 Trustees' Report incorporates the latest change to the Con-

sumer Price Index, that was introduced earlier this year by the Bureau of Labor Statistics which is using the geometric weighting formula, the 1999 Trustees' Report is the baseline that we are operating under for the projections that we have made for all but, unfortunately, one of the plans here—there is one that we did not get a chance to update, Senator Moynihan's plan.

So all changes that have, been implemented to this point, by the Bureau of Labor Statistics are reflected in the baseline estimates for the 1999 Trustees' Report. We did not make any assumptions of any further changes except where indicated within proposals.

Mr. McCRERY. Do you have any thought as to the likelihood of the BLS making further changes to the cost-of-living adjustment?

Mr. GOSS. The only other change really related to the issue of the CPI that I am aware of, that BLS has been talking about, is something referred to as the upper level substitution bias, where there would be the possibility of creating a different kind of formula, referred to as the superlative formula, which would eliminate this one remaining kind of bias which exists in the Consumer Price Index.

I believe that the Bureau of Labor Statistics has announced that they are planning on developing an alternative index to the current CPI, and they should be out in the year 2001 or 2002 with that alternative index.

As we understand it though, that alternative index will not be a modification of the current CPI and therefore will not automatically become the basis for cost-of-living adjustments under Social Security. It would require legislation to effect that change.

Mr. McCRERY. Thank you.

Mr. SHAW. Mrs. Thurman.

Mrs. THURMAN. Thank you, Mr. Shaw.

Mr. Goss, in the Archer-Shaw plan, they are achieving a 75-year solvency by depositing the general revenue equal to 2 percent of taxable payroll into individual accounts and then having that invested by 60 percent of such accounts would be invested in stocks and 40 percent would be invested in bonds.

Could we—then there is the issue of some of the administrative costs and other things that could happen. Could we not do the same thing basically to what has been talked about and achieve this, some of this solvency, by putting this investment in without having administrative costs and doing individual accounts?

Mr. GOSS. If I understand correctly, what you are suggesting is accomplishing the same thing by having 2 percent of taxable payroll transferred from the general fund of the Treasury, not to individual accounts but directly to the Social Security Trust Fund?

Mrs. THURMAN. Correct.

Mr. GOSS. First of all, that is essentially what Representative Stark's proposal was. And as you have seen, actually 2.07 percent, to be a little bit more precise, of taxable payroll over the next 75 years would be sufficient to meet solvency if it were transferred on a year-by-year basis to the trust funds.

If I understand you correctly though, your question involves not only the transfer of those moneys to the Social Security Trust Funds but also to then invest them in a manner similar to what

is being done for the individual accounts under the Archer-Shaw plan.

That clearly would result in an even greater extent of positive actuarial balance than we have under the Stark plan as we stand now.

And there are really two reasons for that, that putting the money directly into the trust funds and investing in stocks, for example, at least a portion of it, would potentially have a more positive effect than having it go into the individual accounts over the 75-year period.

First of all is the one you mentioned. The administrative expenses from the individual accounts.

Mrs. THURMAN. Which could be as high as how much of the investment?

Mr. GOSS. Well, as Chairman Archer and Mr. Shaw mentioned, there is a stipulation in their plan that says there could be a charge of no more than 25 basis points, or one quarter of 1 percent of assets in individual accounts per year. And on the basis of assuming that was the charge, we made the estimate. And as you heard earlier from another Member of the Committee that would still result in an expectation of more than a 5 percent real yield on the trust funds—actually 5.35 percent real yield was the expectation.

If, instead, we were to have the trust funds invested 60 percent in stocks and 40 percent in corporate bonds under the assumptions that had been made, we would expect the yield to be somewhat higher, and the reason being, really, because of the cost of maintaining the individual accounts and maintaining the records.

And this is as indicated, not an enormous cost, and the situation would result in what would be potentially a 5.6 percent yield dropping to about the 5.35 percent yield.

The other thing that I think is really more important to focus on in terms of the potential effect over the 75-year period is the timing of having the money available to the Social Security system. If the money were put directly into the system for each of the next 75 years, then at the end of 75 years, the trust fund would hold the entirety of the transfers of 2 percent made over the 75-year period. In contrast, under the Archer-Shaw plan, a portion of that money that had been transferred from the general fund to individual accounts would still be held in individual accounts and not yet transferred back to the Social Security Trust Funds although I would hasten to mention that it is fair to say that while that would not come within the 75-year valuation period, that is money that would be standing there in those individual accounts under the proposal and would represent a commitment of money for the trust funds into the future.

So I think what we would see in terms of the 75-year valuation period is that the trust fund status would definitely look better from the point of view of putting the money directly into the trust funds.

What we would have to keep in mind is that there would be a large "outside-the-trust funds balance" in the individual accounts under the Archer-Shaw plan.

Mrs. THURMAN. That's all I have. Thank you.

Mr. SHAW. Mr. Hulshof.

Mr. HULSHOF. Thank you, Mr. Chairman. And if you will permit me to maybe delve a little bit into a politically incorrect area—I hope not.

Let me, in anticipation of my question, Mr. Goss, let me again reiterate what Chairman Archer has already said, you have done, and your staff, have done yeoman's work in evaluating all these plans. And for those who may not be aware that the ground rules, if you will, for these 2 days of hearings have been anybody who has got an idea or plan that meets the 75-year, long-term solvency and it had to be submitted by a date certain. And the last day or say, another Congressman, Mr. Kasich of Ohio, has talked about a plan, and unfortunately was not able at least to submit it for our consideration by the time deadline that we had asked.

Let me ask you, have you been able to do the long-term solvency question on Mr. Kasich's plan or is that something in progress?

Mr. GOSS. That is something in progress at this point.

Mr. HULSHOF. And when might we know from you and your office as to whether or not it meets that 75-year long-term solvency test?

Mr. GOSS. We are hopeful of completing that analysis by the end of this week or, by the very latest, early next week.

Mr. HULSHOF. OK.

[The following was subsequently received:]

SOCIAL SECURITY

MEMORANDUM

Date: June 14, 1999 Refer To: TCC

To: Harry Ballantyne
Chief Actuary

From: Stephen C. Goss
Deputy Chief Actuary

Subject: Estimated Long-Range OASDI Financial Effect of Proposal by Representative John Kasich-INFORMATION

This memorandum provides the estimated effect on long-range OASDI financial status of a proposal developed for Representative John Kasich. Specifications for this proposal have been provided by Steve Robinson of Representative Kasich's staff.

This proposal would consist of two parts. The first is a gradual, across-the-board reduction in the rate of growth in the OASDI benefit level from that scheduled under present law. The second is an irrevocable option to accept a further reduction in OASDI benefit level in return for having between 1.0 and 3.5 percent of percent OASDI taxable earnings contributed to an individual account. For those who exercise the option, contributions to the Personal Savings Accounts (PSAs) would be financed by redirecting the appropriate percentage of the worker's OASDI payroll tax from the OASDI Trust Funds to the PSA. In order to maintain solvency for the OASDI Trust Funds, amounts roughly equal to the present value of expected reductions in OASDI benefit payments from the option would be loaned from the General Fund of the Treasury to the Trust Funds for each year, starting 2000, as long as needed. The loans would be repaid with interest at the trust-fund special issue bond yield later.

The first part of the proposal would modify the OASDI benefit formula so that benefit levels would tend to rise from one generation to the next at the rate of growth in consumer prices. Under current law, benefit levels tend to rise at the rate of growth in the average wage level from one generation to the next. Future growth in the average wage level is assumed to average 4.2 percent per year for the

intermediate assumptions of the 1999 Trustees Report. Future growth in consumer prices is assumed to average 3.3 percent. Benefit levels for those newly eligible in 2050 would be expected to be reduced by about 35 percent, and by about 48 percent for those newly eligible in 2075. Under these assumptions, this provision alone would expected to eliminate the currently projected actuarial deficit and restore solvency for OASDI for the indefinite future.

The second part of the proposal would provide an irrevocable option to accept a further benefit reduction in return for a Government-financed contribution to an individual account for workers who will reach age 55 after December 31, 2000. The decision of whether or not to exercise this option would, for workers in their 40's up to age 54 in 2000, be complicated. Married workers, particularly those with only one earner, would be less inclined to exercise the option. Younger workers in 2000, and later, would be increasingly more inclined to exercise the option due to the reduced OASDI benefit levels provided in the first part of the proposal.

If all eligible workers were to exercise the option in 2000 or later, at their earliest opportunity, the specified annual loans from the Treasury to OASDI program would be needed through the year 2045, with repayment expected to begin in the year 2060. With the loans, the OASDI Trust Funds would be expected to remain solvent throughout the long-range period and beyond, under the intermediate assumptions of the 1999 Trustees report. While it is not possible to anticipate the level of voluntary participation in the second part of the proposal, it appears that the OASDI program would be returned to long-range solvency under any reasonable pattern of participation.

The balance of this memorandum provides a description and analysis of the proposal provisions, and estimates of the long-range financial effects of the proposal on the OASDI program. All estimates are based on the intermediate assumptions of the 1999 Trustees Report.

Summary of Proposal Provisions

Part 1. PIA Formula Change

The primary insurance amount (PIA) benefit formula determines the full, unreduced monthly benefit amount for worker beneficiaries. The PIA is subject to actuarial reduction for benefit entitlement before reaching the normal retirement age (NRA, currently 65) and, for retired worker beneficiaries, a delayed retirement credit for postponing benefit entitlement until after the NRA. Benefit levels are increased by the annual cost-of-living adjustment (COLA) after initial benefit eligibility.

The PIA formula consists of three brackets which are separated by two " bend points" . For beneficiaries newly eligible in 1999 these bend points are $505 and $3,043. These bend points are indexed from year to year by the increase in the Social Security average wage indexing series (AWI). A worker's PIA is calculated as 90 percent of the first $505 of career-average indexed monthly earnings (AIME), plus 32 percent of any AIME amount between $505 and $3,043, and 15 percent of any AIME amount in excess of $3,043. Thus, the current-law formula results in PIA benefit levels that tend to rise with the increase in the AWI from one generation to the next.

The first provision of this proposal would modify the PIA formula so that the level of benefits would tend to rise with the growth in consumer prices rather than with the average wage (AWI) from one generation to the next. This would be accomplished by adjusting the 90, 32, and 15 percent factors to *remove* any real growth in the average wage from the increase in benefit levels from one generation to the next.

Specifically, the PIA factors (90, 32, and 15) would be successively reduced each year by the ratio of C to W, where

C = (CPI-W for year-2 / CPI-W for year -3) and
W = (AWI for year-2 / AWI for year-3).

These reductions would be computed beginning with the year 2001, but would be first applied to beneficiaries becoming eligible in 2008. For beneficiaries becoming eligible in 2008, the PIA would be reduced by the total real growth in the AWI from 1998 to 2006. For new eligibles in 2009, the PIA

would be further reduced by the real growth in thew AWI between 2006 and 2007.

Under the intermediate assumptions of the 1999 Trustees Report, the CPI-W is assumed to increase at an average rate of 3.3 percent per year, and the AWI by an average of 4.2 percent per year. Thus the provision would successively slow the growth in benefit levels between generations by about 0.86 percent per year, on average (1.033/1.042 = 0.9914). The first beneficiaries affected, those newly eligible in 2008, would have benefits reduced by an expected 6.7 percent, from the level anticipated under present law (note that this would be lower than the 2008 benefit for a similar worker, one year older, who had retired in 2007 and could be referred to as a " notch"). The size of the reduction would increase for new eligibles in later years.

Part 2. Voluntary Option for the Personal Security Account

This provision would provide workers who will reach age 55 after December 31, 2000 (i.e., those born in 1946 or later) an irrevocable option to have Government-financed contributions made to a Personal Savings Account (PSA) on their behalf. For those who exercise the option, IA contributions would commence as early as the year 2000. However, eligible workers could decide to opt in at any time after 2000 if they choose. In addition, workers who first enter the workforce after 2000 would have the option to (1) start the PSA immediately, (2) delay the start of PSA contributions to a later year, or (3) never opt for the PSA. (Note that opting for the PSA has specific implications for the level of benefits payable from the OASDI program; this is discussed in the next section.)

Contributions each year would depend on the level of the worker's OASDI taxable earnings for the year. The PSA contribution would be equal to

3.5% - 2.5% X (Worker's annual earnings/taxable maximum)

Thus, for a worker with maximum taxable earnings in 2000, projected to be $76,200, the PSA contribution would be 1 percent of annual earnings, or $762. For a worker with earnings at half the taxable maximum, or $38,100, the PSA contribution would be 2.25 percent, or $857. The highest

dollar level of PSA contribution would occur for workers with earnings at 70 percent of the taxable maximum, or $53,340. See the attached Table 1 for more examples. Of course, the PSA contribution would vary throughout each worker's career as a percentage of their annual earnings, as their annual earnings vary relative to the taxable maximum.

PSA contributions for each year would be invested collectively in a money-market account until individual earnings records are reconciled late in the following year. At that point, PSA contributions would be credited to individual PSA accounts. The nature of PSA accounts would apparently be similar to the Federal Government employee Thrift Savings Plan (TSP) in order to keep administrative expenses as low as possible.

Part 2. Benefit Reduction for Those Who Opt for the PSA

For those who opt for the PSA contributions, the level of all OASDI benefits that would be payable based on the worker's earnings will be reduced, beyond reductions from part 1 of the proposal. The reduction is 1/3 percent for each year starting with the year of first PSA contribution and ending with the year prior to first benefit entitlement (regardless of the number of years for which the worker had earnings). Thus, for a worker who opted into the PSA at age 22 and retires at age 62, benefits would be reduced by 13 1/3 percent

Reduction = 1/3% x (62-22) = 13 1/3%

The reduction for a disabled worker beneficiary would generally be smaller, because benefit entitlement generally begins before age 62. The average age at benefit entitlement for disabled worker beneficiaries is about 49, implying an average reduction of 9 percent for those who opt for the PSA starting at age 22. For disabled workers who are converted to retired worker status at their NRA, the lower reduction computed at disabled worker entitlement would continue to apply. Smaller reductions would similarly apply to benefits based on the earnings of workers who die before attaining eligibility for a retired worker benefit (before age 62).

Part 2. Borrowing from and Repaying the General Fund

Because PSA contributions would be financed by redirection the appropriate portion of each participating worker's OASDI payroll tax to the PSA, income to the OASDI program would be substantially reduced for many years before benefit reductions under the optional part 2 become large. Under the proposal, annual loans to the OASDI Trust Funds from the General Fund of the Treasury would be made beginning in the year 2000, for as long as needed to assure that the projected assets in the combined OASDI Trust Funds would never fall below 100 percent of the annual cost of the program.

The amount loaned each year would be 11 percent of the annual benefit cost for the year. This is approximately the present value of the expected future reductions in OASDI benefit payments that would be incurred based on participation in the optional part 2 of the proposal for that year.

Repayment of the loans would commence when the trust fund assets are projected to begin rising steadily above 100 percent of annual cost. Repayments would be scheduled to maintain the trust fund assets at about 100 percent of program annual cost. When the loans have been fully repaid, with interest, the OASDI payroll tax rates could be reduced.

Analysis of Incentives to Exercise the Voluntary Option

Because the benefit reduction in part 2 of the proposal produces a 1/3 percent reduction in lifetime OASDI benefits for every year starting with the election of the PSA up to benefit entitlement, workers will consider carefully whether and when they should enroll. For young workers, particularly students, with very low earnings, it may be financially disadvantageous to enroll for the PSA. For example, a 20-year old student with $1,000 earnings in 2000 would have $34.67 deposited in his/her PSA account, at the cost of a 1/3-percentage-point reduction in lifetime OASDI benefits. Thus, workers may tend to wait to opt into the PSA plan until they have entered full-time employment.

Another group that might consider the option carefully would be workers who are in their mid 40's up to age 54 in 2000. These individuals will have fewer years for PSA contributions

to accumulate enough to offset the benefit reduction. These older workers will also already generally know what their eventual marital status is likely to be at retirement. For those who expect to retire with a spouse who had little or no paid employment, the benefit reduction on benefits for both spouses, including survivor benefits, is more likely to be larger than the potential gain from the PSA, than would be the case for a single worker or a 2-earner married couple.

Tables 2a and 2b, attached, provide comparisons of the reduction in OASI benefit with the value of an annuity from the PSA, assuming investment is half-stock/half-bonds or all bonds, respectively. Values in italics compare reductions in benefits under the optional Part 2 only with the value of the PSA annuity as a percentage of the benefit under the proposal reflecting the reductions from the universally-applied Part 1. These italicized values represent the comparison relevant to choosing whether or not to opt into Part 2 of the proposal.

The table below provides the approximate ages of married individuals in 2000, by earner status, who would be expected to be better off NOT opting for Part 2, assuming an expectation of a 7 percent real yield on stock and 3 percent on long-term U.S. Government bonds. All single workers who expect to remain single would be better off opting for Part 2.

Ages of Workers in 2000 Who Would Expect to Be Better Off NOT Opting for Part 2 of the Kasich Proposal

	Expected PSA Portfolio Return			
	All Long-Term U.S. Govt Bonds		Half Stock Half Bonds	
	2-Ernr	1-Ernr	2-Ernr	1-Ernr
Low Earners	--	48-54	--	52-54
Medium Earners	--	51-54	--	54
High Earners	--	45-54	--	53-54
Maximum Earners	54	34-54	--	43-54

Married 1-earner couples (and 2-earner couples with very low career earnings for the lower earner) who are between about

age 50 and 54 in the year 2000 should be expected not to opt into Part 2 of the proposal. The determination of whether to opt in will depend on how the couple expects to invest the PSA until benefit entitlement, and their level of aversion to risk. Workers in their 50's may still opt for Part 2 if they are willing to invest aggressively (more than half in stock) and are willing to accept the risk that the market will not perform up to expectations. On the other hand, workers in their 40's (or even 30's with very high earnings) who would invest conservatively and prefer a " safer bet" will be more likely to decline to participate in Part 2. As the italicized values in Tables 2a and 2b illustrate, however, all workers in their 20's in the year 2000, and those who enter the workforce after 2000 would be expected to participate in Part 2.

The examples presented in Tables 2a and 2b represent workers with four different earnings levels, and three different marital statuses. Workers with low, medium, and high career earnings have lifetime earnings patterns that reflect the relative earnings levels by age and the probability of having earnings by age for OASDI covered workers in recent years.

The level of earnings for these examples results in an AIME (average indexed monthly earnings) that is equal to that for a steady worker with earnings each year equal to:
(a) the SSA average wage indexing series (AWI) for the medium worker,
(b)45 percent of the AWI for the low worker, and
(c) 160 percent of the AWI for the high worker.
The AWI for 1999 is estimated to be $29,732. The steady maximum worker is assumed to have earnings equal to the Social Security taxable maximum amount ($72,600 for 1999).

The marital statuses are:
(1) single, never married,
(2) married 2-earner couple, meaning both spouses have career earnings averages at the same level, and (3) married 1-earner couple. All married couples are assumed to be the same age in the examples.

An additional consideration for worker participation in Part 2 would be when to become entitled to for benefits. Because the counting of years for benefit reduction under Part 2 ends with the year prior to benefit entitlement, it would generally be advantageous to become entitled as soon as possible, at age 62

for retired worker benefits. The additional PSA contributions after age 62 would be unlikely to be sufficient to offset the 1/3-percentage-point reduction in benefits that would result. It is assumed that both PSA contributions and further benefit reductions under Part 2 would cease after initial benefit entitlement. In this case, workers would be expected to become entitled for benefits at their earliest eligibility, by stopping or decrease work temporarily, if necessary.

Expected Effects on Total Benefits from OASI and PSA

Tables 2a and 2b also illustrate the expected effects of the proposal on total benefit levels. The column labeled " Part 1: Reduction in PIA" illustrates the percentage reduction in the present-law OASI retirement and survivors benefits for workers by age cohort. For those reaching age 65 in 2070, the universal reduction from Part 1 would be 44 percent.

The column labeled " Total Reduction" illustrates the total reduction in OASI benefit from Parts 1 and 2 of the proposal. The total reduction would amount to 52 percent of the present law benefit for those age 65 in 2070. However, those opting for Part 2 will also receive an annuity from the accumulation of their PSA. The columns to the right of each table, labeled " Value of Annuity … As a Percentage of Present Law Benefit" illustrate the comparable value of the PSA accumulation.

These tables show that very young workers (age 20-30) in 2000 who never marry, or marry someone with a fairly similar lifetime earnings record, may expect to have slightly higher retirement benefits if they (1) opt for Part 2, (2) invest fairly aggressively (at least half in stock), and (3) experience investment yields that at least match expectations. Workers will expect to have lower total retirement benefits from OASI and PSA if they (1) are older than 30 in 2000, (2) reach age 20 after about 2015, (3) retire as a member of a 1-earner couple, or a couple with very different levels of lifetime earnings, (4) invest conservatively, or (5) experience investment yields that fall short of expectations.

As noted earlier, benefit reductions under Part 1 would first affect retirees eligible at age 62 in 2008 (age 65 in 2011, as

in Tables 2a and 2b). This initial effect would be a benefit reduction of about 6.7 percent, as compared with no reduction for workers eligible in 2007 or earlier. This would result in a small notch (lower benefit payments in 2008 for new eligibles in 2008 than for similar workers who are 1-year older and were eligible in 2007). This small discrepancy would, at best be only partially offset by participation in Part 2 by those who will reach age 62 in 2008, and would be increased for many.

Long-Range OASDI Financial Effects

Part 1

Enactment of Part 1 of the proposal would progressively reduce OASDI benefits from the levels specified under present law. The extent of the reduction would allow the OASDI program the adequately financed indefinitely under the intermediate assumptions of the 1999 Trustees Report. With Part 1 alone (assuming no one opted for Part 2) the OASDI actuarial balance would be improved by an estimated 2.30 percent of effective taxable payroll, to a positive balance of about 0.24 percent of payroll. The assets of the combined OASDI trust funds would rise to a peak of 383 percent of annual program cost in 2016, then decline to a low of 192 percent of annual cost in 2047, and rise thereafter (as benefit levels continue to decline relative to present law), reaching an estimated 427 percent of annual cost at the end of the 75-year period. See table 4 for details.

It should be noted that under Part 1 of the proposal the financial status of the OASDI program would be considerably more sensitive to the level of real wage growth than under present law. If the real wage differential falls short of the 0.9 percentage point assumed for the intermediate projections of the 1999 Trustees Report, the growth in benefit levels would be reduced to a much smaller extent under Part 1. At the extreme, if the real wage differential averaged 0.0 percentage point (the average wage grows at the same rate as the CPI, on average) Part 1 would provide no savings for the OASDI program, and the long-range OASDI actuarial deficit would be about 3 percent of payroll.

Part 2

If, in addition to enactment of Part 1, *all* eligible workers (under 55 on December 31, 2000) opted for Part 2 of the proposal, the specified borrowing from the General Fund of the Treasury would be required for years 2000 through 2045. This borrowing, equal to 11 percent of OASDI benefit cost each year, would assure that the combined OASDI Trust Funds would not fall below 100 percent of annual cost, under the intermediate assumptions of the 1999 Trustees Report.

With repayment of the loans commencing in 2060, when the trust fund assets would otherwise begin to rise above 100 percent of annual cost, the OASDI long-range actuarial balance would be estimated to be 0.00 percent of taxable payroll. The assets of the combined OASDI trust funds would rise to a peak of 319 percent of annual program cost in 2013, then decline to 106 percent of annual cost in 2060, and stay at about 100 percent of annual cost thereafter (as repayment rates are adjusted to maintain this trust fund ratio). Repayment to the General Fund would be expected to be equal to 0.20 percent of OASDI taxable payroll for 2060 to 2064, 0.35 percent of payroll for 2065 to 2069, and 0.70 percent for 2070 to 2074. The repayment rate would continue to grow after 2074 due to the decreasing cost of the OASDI program, under the intermediate assumptions of the 1999 Trustees Report. See table 3 for details of the expected financing of OASDI under the proposal

However, it is unlikely that all eligible workers would opt for Part 2, as suggested in the earlier section of this memorandum, " Analysis of Incentives to Exercise the Voluntary Option" . It is likely that most workers age 50 to 54 in 2000 and some as young as 30 would choose not to participate in Part 2.

Any lack of participation by older workers in 2000 would tend to have a small negative effect on OASDI financial status as compared with universal participation. The present value of the potential further benefit reduction of Part 2 for these workers would generally be greater than the potential payroll-tax carveout. Thus, nonparticipation of these older workers would reduce the General Fund loan by more than the payroll-tax carveout over the next 2 decades. In addition, some part-time employment early in career would likely not be included in Part 2 benefit reduction because workers might choose to

opt into the plan only after becoming employed on a full-time basis.

Even with the likely reduction in Part 2 participation, the OASDI program would be expected to be adequately financed indefinitely. The net effects of selective nonparticipation would be small and would be accommodated by extending the period of annual loans. If necessary, the size of loans could be increased above 11 percent of taxable payroll.

As described under financial effects of Part 1 alone, above, the OASDI program would be very sensitive to the real wage differential under this proposal.

Stephen C. Goss

Attachments

Table 1. PSA (Kasich) Contribution for Workers in 2000

Level of Annual OASDI Taxable Earnings	PSA Contribution as a Percentage of Earnings	PSA Contribution in Dollar Amount
$1,000	3.47%	$34.67
5,000	3.34%	166.80
10,000	3.17%	317.19
20,000	2.84%	568.77
30,000	2.52%	754.72
40,000	2.19%	875.07
50,000	1.86%	929.79
60,000	1.53%	918.90
70,000	1.20%	842.39
76,200 (taxable maximum)	1.00%	762.00
13,784 (Low = 45% of AWI	3.05%	420.09
30,630 (Average = AWI)	2.50%	764.24
38,100 (1/2 taxable maximum)	2.25%	857.25
49,008 (High = 160% of AWI	1.89%	927.29
53,340 (MaxContrib=0.7xTMax)	1.75%	933.45

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Table 2a. Comparison of Potential PSA annuities with OASI Benefit Reduction for Kasich Proposal
For Worker Opting in 2000 (Age 21 if later) and Investing Half Stock/Half U.S. Bonds until Annuitization at Benefit Entitlement
Assume 0.1 % Annual Administartive Expense on PSA Account Balances

Earnings Scale for Low, Medium, High Earners

		Percentage Reduction in OASDI Benefit			Value of Annuity from PSA Contributions for Steady Workers by Marital Status					
					As a Percentage of Part 1. Benefit			As a Percentage of Present Law Benefit		
Year Entitled at Age 65	Age At Opting into PSA	Part 1: Reduction in PIA	*Part 2: Reduction for PSA*	Total Reduction	*Single*	*Married 2-Earner*	*Married 1-Earner*	Single	Married 2-Earner	Married 1-Earner
Low Earners--Career-Average $13,380 for 1999										
2011	54	6.7	*3.7*	10.1	*5.3*	*5.0*	*3.3*	5.0	4.6	3.1
2020	45	13.8	*6.7*	19.5	*14.4*	*13.3*	*9.0*	12.4	11.5	7.7
2030	35	20.9	*10.0*	28.8	*32.4*	*30.1*	*20.3*	25.6	23.8	16.1
2040	25	27.5	*13.3*	37.2	*56.2*	*52.3*	*35.3*	40.8	37.9	25.6
2050	21	33.5	*14.7*	43.3	*67.9*	*63.2*	*42.7*	45.2	42.0	28.4
2060	21	39.0	*14.7*	48.0	*74.1*	*69.0*	*46.6*	45.2	42.0	28.4
2070	21	44.1	*14.7*	52.3	*80.8*	*75.2*	*50.8*	45.2	42.0	28.4
Medium Earners--Career-Average $29,732 for 1999										
2011	54	6.7	*3.7*	10.1	*6.0*	*5.5*	*3.7*	5.6	5.2	3.5
2020	45	13.8	*6.7*	19.5	*15.4*	*14.3*	*9.6*	13.2	12.3	8.3
2030	35	20.9	*10.0*	28.8	*34.2*	*31.7*	*21.4*	27.0	25.1	17.0
2040	25	27.5	*13.3*	37.2	*60.3*	*56.1*	*37.9*	43.7	40.7	27.5
2050	21	33.5	*14.7*	43.3	*73.9*	*68.8*	*46.4*	49.1	45.7	30.9
2060	21	39.0	*14.7*	48.0	*80.6*	*75.0*	*50.6*	49.1	45.7	30.9
2070	21	44.1	*14.7*	52.3	*87.9*	*81.8*	*55.2*	49.1	45.7	30.9
High Earners--Career-Average $47,572 for 1999										
2011	54	6.7	*3.7*	10.1	*5.6*	*5.2*	*3.5*	5.2	4.8	3.2
2020	45	13.8	*6.7*	19.5	*13.3*	*12.4*	*8.3*	11.5	10.7	7.2
2030	35	20.9	*10.0*	28.8	*28.9*	*26.8*	*18.1*	22.8	21.2	14.3
2040	25	27.5	*13.3*	37.2	*52.7*	*49.0*	*33.1*	38.2	35.5	24.0
2050	21	33.5	*14.7*	43.3	*66.2*	*61.6*	*41.6*	44.0	41.0	27.7
2060	21	39.0	*14.7*	48.0	*72.2*	*67.2*	*45.4*	44.0	41.0	27.7
2070	21	44.1	*14.7*	52.3	*78.8*	*73.3*	*49.5*	44.0	41.0	27.7
Steady Maximum Earners--$72,600 for 1999										
2011	54	6.7	*3.7*	10.1	*4.5*	*4.1*	*2.8*	4.2	3.9	2.6
2020	45	13.8	*6.7*	19.5	*10.2*	*9.5*	*6.4*	8.8	8.2	5.5
2030	35	20.9	*10.0*	28.8	*21.9*	*20.4*	*13.8*	17.3	16.1	10.9
2040	25	27.5	*13.3*	37.2	*39.9*	*37.1*	*25.1*	28.9	26.9	18.2
2050	21	33.5	*14.7*	43.3	*51.9*	*48.3*	*32.6*	34.5	32.1	21.7
2060	21	39.0	*14.7*	48.0	*56.6*	*52.7*	*35.6*	34.5	32.1	21.7
2070	21	44.1	*14.7*	52.3	*61.8*	*57.5*	*38.8*	34.5	32.1	21.7

Based on intermediate assumptions of the 1999 Trustees Report, and assumed 7% real stock yield
Assume 3% net real annuity yield (CPI-Indexed; Unisex single or Joint and 2/3 Survivor)

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Table 2b. Comparison of Potential PSA annuities with OASI Benefit Reduction for Kasich Proposal
For Worker Opting in 2000 (Age 21 if later) and Investing ALL U.S. Bonds until Annuitization at Benefit Entitlement
Assume 0.1 % Annual Administartive Expense on PSA Account Balances *Earnings Scale for Low, Medium, High Earners*

Year Entitled at Age 65	Age At Opting Into PSA	Percentage Reduction in OASDI Benefit: Part 1: Reduction in PIA	*Part 2: Reduction for PSA*	Total Reduction	Value of Annuity from PSA Contributions for Steady Workers by Marital Status — *As a Percentage of Part 1. Benefit*: *Single*	*Married 2-Earner*	*Married 1-Earner*	As a Percentage of Present Law Benefit: Single	Married 2-Earner	Married 1-Earner
Low Earners--Career-Average $13,380 for 1999										
2011	54	6.7	*3.7*	10.1	*4.7*	*4.3*	*2.9*	4.4	4.0	2.7
2020	45	13.8	*6.7*	19.5	*11.4*	*10.6*	*7.1*	9.9	9.2	6.2
2030	35	20.9	*10.0*	28.8	*22.9*	*21.3*	*14.4*	18.1	16.8	11.4
2040	25	27.5	*13.3*	37.2	*35.5*	*33.1*	*22.3*	25.8	24.0	16.2
2050	21	33.5	*14.7*	43.3	*41.5*	*38.7*	*26.1*	27.6	25.7	17.4
2060	21	39.0	*14.7*	48.0	*45.3*	*42.2*	*28.5*	27.6	25.7	17.4
2070	21	44.1	*14.7*	52.3	*49.4*	*46.0*	*31.1*	27.6	25.7	17.4
Medium Earners--Career-Average $29,732 for 1999										
2011	54	6.7	*3.7*	10.1	*5.2*	*4.8*	*3.3*	4.9	4.5	3.0
2020	45	13.8	*6.7*	19.5	*12.3*	*11.4*	*7.7*	10.6	9.8	6.6
2030	35	20.9	*10.0*	28.8	*24.3*	*22.6*	*15.2*	19.2	17.8	12.0
2040	25	27.5	*13.3*	37.2	*38.1*	*35.4*	*23.9*	27.6	25.7	17.3
2050	21	33.5	*14.7*	43.3	*45.0*	*41.9*	*28.3*	29.9	27.8	18.8
2060	21	39.0	*14.7*	48.0	*49.1*	*45.7*	*30.8*	29.9	27.8	18.8
2070	21	44.1	*14.7*	52.3	*53.5*	*49.8*	*33.6*	29.9	27.8	18.8
High Earners--Career-Average $47,572 for 1999										
2011	54	6.7	*3.7*	10.1	*4.9*	*4.6*	*3.1*	4.6	4.3	2.9
2020	45	13.8	*6.7*	19.5	*10.8*	*10.0*	*6.7*	9.3	8.6	5.8
2030	35	20.9	*10.0*	28.8	*20.7*	*19.2*	*13.0*	16.4	15.2	10.3
2040	25	27.5	*13.3*	37.2	*33.2*	*30.9*	*20.9*	24.1	22.4	15.1
2050	21	33.5	*14.7*	43.3	*40.0*	*37.2*	*25.1*	26.6	24.7	16.7
2060	21	39.0	*14.7*	48.0	*43.6*	*40.6*	*27.4*	26.6	24.7	16.7
2070	21	44.1	*14.7*	52.3	*47.6*	*44.3*	*29.9*	26.6	24.7	16.7
Steady Maximum Earners--$72,600 for 1999										
2011	54	6.7	*3.7*	10.1	*3.9*	*3.7*	*2.5*	3.7	3.4	2.3
2020	45	13.8	*6.7*	19.5	*8.3*	*7.7*	*5.2*	7.1	6.6	4.5
2030	35	20.9	*10.0*	28.8	*15.7*	*14.6*	*9.9*	12.4	11.6	7.8
2040	25	27.5	*13.3*	37.2	*25.2*	*23.4*	*15.8*	18.3	17.0	11.5
2050	21	33.5	*14.7*	43.3	*31.1*	*29.0*	*19.6*	20.7	19.2	13.0
2060	21	39.0	*14.7*	48.0	*33.9*	*31.6*	*21.3*	20.7	19.2	13.0
2070	21	44.1	*14.7*	52.3	*37.0*	*34.4*	*23.3*	20.7	19.2	13.0

Based on intermediate assumptions of the 1999 Trustees Report, and assumed 7% real stock yield
Assume 3% net real annuity yield (CPI-indexed; Unisex single or Joint and 2/3 Survivor)

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Table 3 a Kasich Proposal: All Opt for PSA; Borrow and Repay Gen Fund IA Cntrb 2 %, Ben Offset 0.0 %
With Ult Real TF Int Rate of 3.0

Year	Cost Rate	Income Rate*	Annual Balance	TFR 1-1-yr	Marginal Change in OASDI Contrib Rate	Net OASDI Contrib Rate*	Change in OASDI Contrib Rt from-- Carve-out	Borrow & Repay GF
1999	10.79	12.70	1.91	194		12.40		
2000	10.79	12.23	1.44	217	-0.421	11.98	-1.59	1.17
2001	10.83	12.17	1.34	234	-0.082	11.90	-1.68	1.17
2002	10.91	12.15	1.24	249	-0.021	11.88	-1.71	1.16
2003	10.99	12.14	1.15	263	-0.021	11.85	-1.74	1.19
2004	11.08	12.12	1.04	274	-0.019	11.84	-1.77	1.20
2005	11.18	12.11	0.94	284	-0.019	11.82	-1.80	1.21
2006	11.29	12.12	0.83	292	-0.006	11.81	-1.82	1.23
2007	11.41	12.12	0.71	298	-0.005	11.81	-1.83	1.24
2008	11.53	12.13	0.60	304	-0.005	11.80	-1.85	1.25
2009	11.65	12.13	0.48	309	-0.005	11.80	-1.87	1.27
2010	11.77	12.13	0.36	313	-0.005	11.79	-1.89	1.28
2011	11.91	12.14	0.23	316	-0.003	11.79	-1.91	1.29
2012	12.07	12.15	0.08	318	-0.001	11.79	-1.92	1.31
2013	12.24	12.17	-0.07	319	0.010	11.80	-1.93	1.33
2014	12.42	12.20	-0.22	319	0.014	11.81	-1.94	1.35
2015	12.60	12.22	-0.38	318	0.013	11.82	-1.95	1.37
2016	12.79	12.25	-0.54	316	0.015	11.84	-1.95	1.39
2017	12.99	12.28	-0.71	313	0.014	11.85	-1.96	1.41
2018	13.18	12.30	-0.88	308	0.015	11.87	-1.97	1.43
2019	13.38	12.33	-1.05	303	0.014	11.88	-1.97	1.46
2020	13.57	12.36	-1.21	297	0.015	11.90	-1.98	1.48
2021	13.74	12.39	-1.35	290	0.015	11.91	-1.98	1.50
2022	13.88	12.42	-1.47	283	0.012	11.92	-1.99	1.51
2023	14.02	12.44	-1.58	275	0.011	11.94	-1.99	1.53
2024	14.14	12.46	-1.68	267	0.009	11.94	-2.00	1.54
2025	14.24	12.48	-1.76	259	0.007	11.95	-2.00	1.55
2026	14.32	12.49	-1.82	250	0.009	11.96	-2.00	1.56
2027	14.38	12.51	-1.87	241	0.007	11.97	-2.00	1.57
2028	14.41	12.52	-1.89	233	0.004	11.97	-2.00	1.57
2029	14.42	12.53	-1.89	224	0.001	11.97	-2.00	1.57
2030	14.40	12.53	-1.87	215	-0.002	11.97	-2.00	1.57
2031	14.37	12.54	-1.83	207	-0.003	11.97	-2.00	1.57
2032	14.32	12.54	-1.78	199	-0.005	11.96	-2.00	1.56
2033	14.25	12.53	-1.72	191	-0.007	11.96	-2.00	1.56
2034	14.15	12.52	-1.63	184	-0.010	11.94	-2.00	1.54
2035	14.04	12.51	-1.53	177	-0.013	11.93	-2.00	1.53
2036	13.91	12.49	-1.41	172	-0.014	11.92	-2.00	1.52
2037	13.76	12.48	-1.29	166	-0.015	11.90	-2.00	1.50
2038	13.61	12.46	-1.15	162	-0.016	11.89	-2.00	1.49
2039	13.46	12.44	-1.02	158	-0.017	11.87	-2.00	1.47
2040	13.30	12.42	-0.88	156	-0.017	11.85	-2.00	1.46
2041	13.14	12.40	-0.74	154	-0.017	11.84	-2.00	1.44
2042	12.99	12.38	-0.61	153	-0.016	11.82	-2.00	1.42
2043	12.84	12.36	-0.48	153	-0.016	11.80	-2.00	1.40
2044	12.70	12.34	-0.36	154	-0.015	11.79	-2.00	1.39
2045	12.56	12.32	-0.24	156	-0.015	11.77	-2.00	1.37
2046	12.42	10.95	-1.48	159	-1.372	10.40	-2.00	
2047	12.30	10.94	-1.36	151	0.000	10.40	-2.00	
2048	12.18	10.94	-1.24	145	0.000	10.40	-2.00	
2049	12.07	10.94	-1.13	139	0.000	10.40	-2.00	
2050	11.96	10.93	-1.03	134	0.000	10.40	-2.00	
2051	11.87	10.93	-0.93	129	0.000	10.40	-2.00	
2052	11.78	10.93	-0.86	124	0.000	10.40	-2.00	
2053	11.71	10.93	-0.78	121	0.000	10.40	-2.00	
2054	11.63	10.93	-0.70	117	0.000	10.40	-2.00	
2055	11.56	10.93	-0.64	114	0.000	10.40	-2.00	
2056	11.50	10.93	-0.57	112	0.000	10.40	-2.00	
2057	11.44	10.93	-0.51	110	0.000	10.40	-2.00	
2058	11.37	10.93	-0.45	108	0.000	10.40	-2.00	
2059	11.31	10.92	-0.39	107	0.000	10.40	-2.00	
2060	11.25	10.72	-0.53	106	-0.200	10.20	-2.00	-0.20
2061	11.19	10.72	-0.47	104	0.000	10.20	-2.00	-0.20
2062	11.13	10.72	-0.41	103	0.000	10.20	-2.00	-0.20
2063	11.06	10.72	-0.34	102	0.000	10.20	-2.00	-0.20
2064	11.00	10.72	-0.28	101	0.000	10.20	-2.00	-0.20
2065	10.94	10.57	-0.37	101	-0.150	10.05	-2.00	-0.35
2066	10.87	10.57	-0.31	100	0.000	10.05	-2.00	-0.35
2067	10.81	10.56	-0.25	100	0.000	10.05	-2.00	-0.35
2068	10.75	10.56	-0.18	101	0.000	10.05	-2.00	-0.35
2069	10.68	10.56	-0.12	102	0.000	10.05	-2.00	-0.35
2070	10.62	10.21	-0.41	103	-0.350	9.70	-2.00	-0.70
2071	10.56	10.21	-0.35	102	0.000	9.70	-2.00	-0.70
2072	10.50	10.20	-0.29	101	0.000	9.70	-2.00	-0.70
2073	10.44	10.20	-0.24	101	0.000	9.70	-2.00	-0.70
2074	10.38	10.20	-0.18	101	0.000	8.70	-2.00	-0.70

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
1999 -2073	12.47	12.47	0.00	2.07

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
* Includes borrow from and repay to General Fund.

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Table 4 a Kasich Proposal: NONE Opt for PSA IA Cntrb 2 %, Ben Offset 0.0 %
With Ult Real TF Int Rate of 3.0

Year	Cost Rate	Income Rate*	Annual Balance	TFR 1-1-yr	Marginal Change in OASDI Contrib Rate	Net OASDI Contrib Rate*	Change in OASDI Contrib Rt from-- Carve-out	Borrow & Repay GF
1999	10.79	12.70	1.91	194		12.40		
2000	10.79	12.65	1.86	217		12.40		
2001	10.83	12.67	1.85	238		12.40		
2002	10.91	12.68	1.76	258		12.40		
2003	10.99	12.68	1.69	276		12.40		
2004	11.08	12.69	1.61	292		12.40		
2005	11.18	12.70	1.52	307		12.40		
2006	11.29	12.71	1.42	320		12.40		
2007	11.41	12.71	1.31	332		12.40		
2008	11.53	12.73	1.20	343		12.40		
2009	11.67	12.73	1.07	352		12.40		
2010	11.81	12.74	0.94	360		12.40		
2011	11.96	12.75	0.79	368		12.40		
2012	12.15	12.76	0.62	374		12.40		
2013	12.34	12.78	0.43	378		12.40		
2014	12.55	12.79	0.24	382		12.40		
2015	12.77	12.80	0.03	383		12.40		
2016	13.00	12.82	-0.19	383		12.40		
2017	13.24	12.83	-0.41	382		12.40		
2018	13.47	12.85	-0.63	379		12.40		
2019	13.72	12.86	-0.85	375		12.40		
2020	13.95	12.88	-1.07	369		12.40		
2021	14.17	12.89	-1.27	363		12.40		
2022	14.36	12.91	-1.45	356		12.40		
2023	14.54	12.92	-1.62	349		12.40		
2024	14.71	12.93	-1.78	341		12.40		
2025	14.86	12.95	-1.91	332		12.40		
2026	14.99	12.96	-2.03	323		12.40		
2027	15.09	12.97	-2.13	314		12.40		
2028	15.17	12.98	-2.20	304		12.40		
2029	15.23	12.99	-2.24	294		12.40		
2030	15.25	13.00	-2.26	285		12.40		
2031	15.26	13.00	-2.26	275		12.40		
2032	15.25	13.01	-2.24	266		12.40		
2033	15.22	13.01	-2.21	257		12.40		
2034	15.17	13.02	-2.15	248		12.40		
2035	15.08	13.02	-2.06	240		12.40		
2036	14.98	13.02	-1.96	233		12.40		
2037	14.87	13.02	-1.85	225		12.40		
2038	14.75	13.02	-1.73	219		12.40		
2039	14.62	13.02	-1.60	213		12.40		
2040	14.49	13.02	-1.47	208		12.40		
2041	14.36	13.02	-1.34	204		12.40		
2042	14.23	13.01	-1.22	200		12.40		
2043	14.11	13.01	-1.10	197		12.40		
2044	14.00	13.01	-0.99	195		12.40		
2045	13.88	13.01	-0.87	193		12.40		
2046	13.77	13.01	-0.76	193		12.40		
2047	13.66	13.00	-0.66	192		12.40		
2048	13.56	13.00	-0.56	193		12.40		
2049	13.47	13.00	-0.47	194		12.40		
2050	13.38	13.00	-0.38	196		12.40		
2051	13.30	13.00	-0.30	198		12.40		
2052	13.23	13.00	-0.23	201		12.40		
2053	13.17	13.00	-0.17	204		12.40		
2054	13.11	13.00	-0.11	208		12.40		
2055	13.05	13.00	-0.06	212		12.40		
2056	13.00	13.00	0.00	217		12.40		
2057	12.94	13.00	0.05	222		12.40		
2058	12.89	13.00	0.11	228		12.40		
2059	12.83	13.00	0.17	234		12.40		
2060	12.77	13.00	0.22	241		12.40		
2061	12.71	13.00	0.28	249		12.40		
2062	12.65	12.99	0.34	258		12.40		
2063	12.59	12.99	0.41	267		12.40		
2064	12.52	12.99	0.47	277		12.40		
2065	12.45	12.99	0.54	288		12.40		
2066	12.39	12.99	0.60	299		12.40		
2067	12.32	12.99	0.67	312		12.40		
2068	12.25	12.99	0.74	325		12.40		
2069	12.18	12.98	0.80	340		12.40		
2070	12.11	12.98	0.87	355		12.40		
2071	12.04	12.98	0.94	371		12.40		
2072	11.97	12.98	1.00	389		12.40		
2073	11.91	12.98	1.07	407		12.40		
2074	11.84	12.97	1.13	427		12.40		
	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal				
1999 -2073	13.15	13.39	0.24	2.30				

Based on Intermediate Assumptions of the 1999 Trustees Report
With Ult Real Int Rate of 3.00
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Following up on what Mr. McCrery asked, the line of questions he asked, that many of the plans we heard about yesterday have similar benefit adjustments, there is the reduction of the cost-of-living adjustments, increasing the retirement age was mentioned in a couple of the plans, I know there was some discussion yesterday, if I may be permitted to say, some mind-numbing discussion about bend points, extending the period of time over which benefits are calculated, and the like.

Can you tell me or briefly describe the effects of these changes on beneficiaries? And where I would like you to go with this is, are

there groups or types of beneficiaries that might be disproportionately affected by some of these changes, like the COLAs and raising the retirement age?

Mr. GOSS. Let me talk about the cost-of-living adjustment. I think there are really two ways of looking at changing the cost-of-living adjustment. I believe that most Members of Congress who have made proposals for changing the cost-of-living adjustment have done that from the point of view of an expectation and a belief that the Consumer Price Index is overstated in terms of its rate of increase. Therefore, it is probably fair to say, to the extent that that is true, if the cost-of-living adjustment is reduced so that it becomes a more accurate representation of what the true cost of living is, then one could conclude that, in fact, we are not really disadvantaging beneficiaries in the future.

However, looked at from the point of view of the present-law, cost-of-living adjustment versus having a one-third of 1 percent per year or one-half of 1 percent per year reduction in that cost-of-living adjustment, clearly, the effect of that is the longer a person has been eligible for benefits, the more their benefits, relative to present-law levels, will be reduced.

For instance, a one-half of 1-percent reduction in the annual cost-of-living adjustment will leave the beneficiary who has been receiving benefits or who has been eligible to receive benefits for 10 years with about a 4½ to 5 percent lower benefit than they would otherwise get.

On the other hand, a beneficiary who has been receiving benefits or might have been receiving them for as much as 20 years with that one-half of 1 percent per year reduction would be receiving benefits that are on the order of 9 to 10 percent less. And it goes on.

It suggests, obviously, people who have been on the rolls or who have lived the longest, which tend to be women more than men, and often times widows, would be ones somewhat disproportionately affected by cost-of-living adjustments.

Now, on the other item you mentioned, on the retirement age—retirement-age proposals that have been put forth tend to have a very similar percentage reduction in benefit levels for retirement and survivor benefits for all workers, regardless of their age, regardless of their income level.

For instance, a 1-year increase in the normal retirement age, from 65, where it is today, to 66, is already scheduled to occur under current law. People who choose to continue to start receiving benefits at exactly the same age, 62 for example, will receive benefits that will be roughly about 6½ percent lower than if the retirement age were not increased by 1 year. Eventually undercurrent law the retirement age will increase to 67.

And that is regardless of the person's income level or regardless of their benefit level. Everybody would receive about the same percentage reduction.

But from that point of view, it would be fairly equal. From the other point of view, which people will oftentimes look at, from the adequacy of benefit levels, of course you could argue that that might tend to hurt people at the low-income, low-benefit levels more.

But the key point, I think, from the point of Social Security benefits is that the percentage reduction would be the same for everybody.

The one exception, of course, is that increases in the retirement age in general would not affect benefits paid to disabled worker-beneficiaries or their families.

Mr. HULSHOF. Thank you, sir.

Mr. SHAW. Mr. Lewis.

Mr. LEWIS of Kentucky. I have one question, and I would like to know the significance of having the high trust fund balances. Do the trust fund balances represent money that is available to pay the benefits? And I ask that in reference to yesterday's hearings, where Representative Nadler emphasized that at the end of the 75-year period the trust fund ratio under his plan was 786, which, of course, is very high. But in the same year, the Social Security Program is running a cash deficit equal to 5.95 percent of the payroll.

How can the trust fund balances be so high while the cash shortfalls are so large? As we evaluate reform proposals, what weight should we give to trust fund ratios versus the cash flow? The cash flow is something I have been trying to talk about all morning.

Mr. GOSS. Thank you. This really is a very, very important question. And I think to a certain extent it defines the issue of the extent to which almost all of these proposals would move us from the current financing of the Social Security Program, which is essentially on a pay-as-you-go basis. And under a pure pay-as-you-go or current-cost basis, you just have to have the tax income to the program coming in each year equal to the amount of outgo for that year. You don't have any trust fund to draw on.

I believe every one of these proposals, with perhaps one exception, that is, nine out of 10 of these proposals, would move us toward having substantial advance funding for the system.

And I think we should understand the advantages of having advance funding for a system, whether it be Social Security or a private pension plan. All private pension plans are required to have advance funding. Any plan that has substantial advance funding will have exactly this situation where the amount of contributions into the plan each year will be less, in fact, than the amount of money that is coming out.

And, of course, with a large amount of advance funding and with the benefit of the returns that we would realize on the funds being held, this would allow for more money to be paid out than the contributions. And that is because of the yield on those moneys that are in fact invested.

Under Congressman Nadler's plan, we do indeed have a situation where we would have almost 8 times the annual cost of the program being held in the trust funds. In his particular case, I believe it was 30 percent in the form of stocks and 70 percent in the form of bonds. As we discussed earlier, there would be a very high yield on that large amount of money held in the trust funds. Very much less than the entirety of that yield would be needed to be retained in the trust funds to keep its value rising in the future with the rate of growth and the cost of the program, for example meeting this objective of having a constant trust fund ratio.

That would leave, in effect, a lot of the yield on the trust fund from year to year available to pay the current cost of the program, which is exactly what private pensions do.

So I think this is really a natural outgrowth. And whether it is a plan like Congressman Nadler's or any of the plans that would have individual accounts, if we were to look at the entirety of what is happening with the individual accounts plus the Social Security Trust Funds, we would see much the same situation, that we would have a large fund through its yield providing a lot of the income that is needed to pay benefits on a year-to-year basis, thereby lowering the extent to which we have to have tax-rate increases.

Mr. SHAW. Do any of the Members have any other questions?

Mr. Goss, I want to add my compliments to those paid to you by the Chairman with regard to—I know you have certainly been tested for the last few months. And you have certainly come through beautifully, and we appreciate the hard work you are doing. And we certainly hope that we can reward you with a plan that is actuarially sound for 75 years and way beyond.

Thank you.

This hearing is adjourned.

[Whereupon, at 1:29 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

Statement of American Farm Bureau Federation

PRESERVE INTEGRITY OF SOCIAL SECURITY

Farmers and ranchers support the preservation of the Social Security system as a safety net to provide workers and their families retirement income, disability protection or assistance because of the early death of a family wage earner. Farmers and ranchers are concerned, however, about the future and financial soundness of the Social Security system. Farm Bureau believes that reform is needed to preserve the integrity of Social Security for retirees and workers paying into the system.

The average age of farmers and ranchers is now 54 years old. This means that almost half of them are at, or near, retirement age. They are very concerned about the return they will receive on a lifetime's worth of Social Security taxes. The current system is a major portion of their retirement program. They must be able to rely upon Social Security in their retirement years.

Ninety-nine percent of farms are operated by sole-proprietors and or by family partnerships. As self-employed individuals, agricultural producers pay the full 12.4 percent payroll tax, usually as one lump sum along with their income tax payment. They are painfully aware of the high taxes needed to fund the current system and realize the urgency of saving the Social Security system.

CHOICE OF RETIREMENT SYSTEMS

While Farm Bureau supports preserving the Social Security system, we believe people should have the option of contributing to personal retirement systems. For years we have recognized each individual's right to participate in pension plans in addition to Social Security. We believe that people should also be able to invest in private plans within the Social Security framework using the same deposit percentages and withdrawal age rules as the regular Social Security program. People should have the right to choose to stay in the standard Social Security program or shift their Social Security taxes into personal retirement accounts.

PROGRAM FUNDING

We oppose an increase in Social Security taxes. Social Security, either the standard plan or new private retirement plans, should be funded by payroll taxes. We oppose any proposal to finance Social Security retirement income benefits out of general revenue. Social Security taxes should continue to appear as a separate deduction of Federal Insurance Contribution Act (FICA) taxes to make them clearly identifiable.

All employees, both in the private and public sector, should be included in the Social Security program. Employers and employees should continue to share equally in the payment of Social Security taxes. Low-income taxpayers should not be exempted from paying Social Security taxes because of their level of incomes.

Social Security Surplus

Social Security taxes collected should be placed in a restricted interest-bearing fund to be used only for Social Security. Because we support placing Social Security funds in interest bearing accounts and private retirement accounts, we oppose government investment of Social Security Trust Fund money in stocks of private companies.

Benefits

Benefit levels should be preserved for retirees and those that are near retirement and, when in need of adjustment, should be changed based on a percentage of the annual decrease or increase in average wages. Benefits, both in the standard plan and in alternative private plans, should be based on an individual's contribution to the system. We oppose means testing as a way to limiting Social Security benefits for those that have contributed to the system. We oppose earned income restrictions for those receiving Social Security benefits.

Summary

Farm Bureau supports reforms to the Social Security system. The integrity of the system must be maintained for retirees and near retirees while giving workers the opportunity to invest their Social Security taxes in personal retirement accounts. We oppose tax increases and government investment of Social Security Trust Funds in equities markets.

Statement of Wendell H. Eriksson, Minneapolis, Minnesota

Mr. Chairman and Members of the Committee, thank you for the opportunity to submit Testimony regarding plans to reform Social Security.

In the Senate, Mr. Moynihan and Mr. Kerry last January introduced legislation in the form of S. 21 with the objective of reducing Social Security payroll taxes and to assure the long range solvency of the system. In April of this year Chairman Archer and Mr. Shaw introduced legislation also with the intention of remedying the long term solvency of the system. (Indeed, it is the reason for this hearing.) In addition, the Clinton Administration's new Budget offers four options to resolving our Social Security/Medicare dilemmas: using the budget surplus, increasing fertility—i.e., more babies, doubling immigration, and shortening Boomer life spans. That there are varying proposals being laid on the table, suggests the impending calamity confronting this nation if nothing is promptly done to alleviate the systemic problems.

Due to time and space limits, my Testimony will often only indirectly discuss several of these proposals while providing additional background information regarding population growth and the funding of Social Security.

I will begin by first presenting my recommendations, followed by background information on the profound structural program flaws. I then turn to the proposed remedies centering on adding additional enrollees and of population growth with the towering role of immigration in that population growth.

RECOMMENDATIONS

The overarching question is how should Americans provide for their retirement and what is the appropriate role of the government? My response is that the current retirement system should be withdrawn because of its numerous inequities, unconvincing financial benefits, and fundamentally self-destructive program design. Regrettably, previous legislative remedies have only served to postpone the inevitable Social Security/Medicare collapse. The recommendation is to rapidly transition the government's retirement system to an all encompassing private individual retirement account (IRA and/or ROTH type IRA). Proposals to fund Social Security from rapid population growth, especially immigration, are counter productive and ill-advised. Its welfare aspects must be funded from general revenue sources.

The tremendous opportunity cost of not being able to invest in an IRA has been noted elsewhere. Here it is sufficient to say that anyone with an IRA, rather than Social Security, would have had the means and opportunity to have saved and earned a substantial retirement nest egg. For example, if all deposits were to a single comprehensive private individual retirement account, as little as three to five percent of annual wages would provide a very pleasant retirement fund. Even a worker earning as little as $20–$25,000 per year could have at retirement an inflation adjusted pension of around $75,000 per year indefinitely and upon death the balance would go to the family. On the other hand, under the government plan the payments are dramatically less and any remaining amounts are frequently lost to the worker's family. Not only is the Social Security system counterproductive to achieving retirement security, it eliminates or substantially reduces the ability of workers and families to fund their own retirement programs.

Every individual must have a private individual retirement account with deposits from all sources (individual, company, and government sponsored) flowing into it. The IRA (or ROTH type IRA, taxable and non-taxable types as today) is an asset of the individual so the owner has full responsibility for investment decisions (with limitations, as in current IRA's and Keogh plans). Because the goal is an individual's retirement, there should be no age limit for the initial set up nor is an earned income requirement appropriate. Earned or unearned income should be acceptable deposit (as now, only earned income should be tax deductible) and non-owners (i.e., Grandma) should be able to add a non-deductible $500 per year to any person's IRA (and be a gift beyond the reach of the gift or death tax). If under age 35, the maximum annual deposit by the owner should be the greater of $1,000 or 65 X age (adjusted for inflation) while those over 35 should be able to deposit to their IRA 100 X age. Similar to current practices, employers should have the option of matching and depositing 2–3% of an employee's wages each year.

All current workers and retirees in the Social Security retirement program should earn a Social Security annuity based on their past deposits and current rules, and then be removed from further FICA payments or benefits, thus ending the program over time. This is where the proposal to use much of the "budget surplus" to help fund Social Security comes into play. Rather than purchasing government bonds (and continuing the self-destructive cycle only under a different name) those excess funds should be paid now, directly to an individual to retire prior contributions into an individual's IRA, including a return on investment. This "buy-out" process removes the otherwise compounding system liabilities from the system. I recommend it begin with the young worker and move up the age ladder (and everyone should have the option). In this way individuals and associated liabilities are rapidly removed from the system. Without the onerous FICA tax, the ability to fund their own retirement program, and if necessary, to pay a slightly increased income tax rate, is significantly enhanced.

Please note, I am *not* advocating discarding the government welfare function of the safety net, only that it no longer be funded from workers and their families' retirement funds. I would like to now turn to the profound design flaws of the system.

IN TWO FUNDAMENTAL WAYS SOCIAL SECURITY IS SELF-DESTRUCTING

First, it is designed as a pyramid "Ponzi" scheme, and second, there is the false notion of a "trust fund."

PONZI PYRAMID SCHEME

The first self-destructing flaw is that the funding of the Social Security system is that it is a classic Ponzi pyramid scheme. The scheme is named after Charles Ponzi who in the 1920's used the method to defraud investors of millions of dollars. The term is given to any scam that bilks people by promising returns for money invested, but can only do so by using funds received from new participants to pay the earlier contributors, a "pay-as-you-go" system. The scheme is doomed to fail because its pyramid effect requires ever growing numbers of new participants and spiraling sums of money. The Social Security system, like the Ponzi scheme, crumbles from below when the inevitable numbers of new participants is insufficient to support those at the top, the retirees in our case.

The pyramid suggests the necessary demographic shape of a population requiring rapid and unending population growth in order to continue the ill-designed program. This was an absurd assumption then, and in this unsustainabley populated country today is inexcusable. The truth of the matter is that the more people in the retirement system, the more unmanageable and intractable the problems. Any increase in the numbers of people in the system exacerbates the pyramid scheme nature of the system and merely postpones and intensifies the inevitable collapse; the irony

of it is that the fewer enrolled in the program the less harm done and less politically awkward the ensuing remedy.

The proposals to increase enrollees, promote fertility increases, and legislation to open a floodgate of immigration are unseen and little known attempts to remedy the funding dilemma by rapidly increasing numbers at the bottom of the pyramid. This matter applies equally to the additions of workers (e.g., state employees) not now included in the program. The immigration legislation of the last nearly thirty years has been a continuing endeavor to force, in a manner unprecedented in history, population growth in the U.S. to mirror the excessive population growth in the baby-boom era, and as policy, to continue rapid and unrestricted population growth indefinitely.

These proposed and current demographic policies are not environmentally nor economically sustainable, are terribly socially disruptive, and will produce absolute chaos in the Social Security system.

Demographics plays an important role in shielding or aggravating the self-destructive nature of the program. The Social Security cash flow (pension) is generally paid by younger workers (the Ponzi effect) and that an increase in payments is paid by increasing FICA taxes of current workers is a symptom of the funding quicksand upon which the system is based. This observation underlies the motivation to redesign the cost-of-living (COLA) portion of the system in order to reduce annual inflation adjustments. Unfortunately, the process takes advantage of the ignorance of the general public regarding compounding—unknown to an unsuspecting public, even numbers as small as one percent overtime become a very big financial deal!

THE "TRUST FUND"

The second self-destructing design flaw is the notion of a trust fund. In contrast to an IRA, employer funded pension plans, insurance, private annuities, and other pension plans, the Social Security retirement system is not a funded system; in reality there is no fund. To the contrary, there is a future tax increase of unimaginable proportions, a quietly waiting irreversible financial time bomb. The lack of funding is a legal inconsistency between the requirements of all other pension plans and the U.S. government retirement plan for its citizens.

(When hearing the following description, please bear in mind there are proposals to use much of the so-called "budget surplus" to purchase Treasury Bonds to shore up the Social Security Trust Fund. The reality of it is that this proposal is merely a minor change in name and location only. Thus, the dollars remain a government liability with the same, even at a higher rate, compounding interest paid by the taxpayers.)

Let's review the process as simply as possible. The "trust fund" purchases special Congress Treasury Bonds (this helps balance the current budget deficit) that pay interest. This interest is not actually paid into a fund, but is penciled into a ledger as an "IOU." The interest, now IOUs, compound over time. Compounding is a marvelous road to wealth accumulation were the fund an IRA and not a Social Security entity. However, it is circular: increasing interest payments (IOU's) produce increasing FICA taxes but increasing FICA also produces increasing interest payments (IOU's); in turn, increasing taxes, and so on. It is Congress spending now while lending to itself. In fifty years each $1 in the trust fund will compound to about $75 (e.g. Kerrey & Trustee Reports!). The wherewithal necessary to pay those staggering compounding obligations is at the heart of the dilemma.

If one considers the pyramid (Ponzi) nature of the design and then combines it with these massively compounding liabilities one will began to understand the magnitude of the design mistakes. Increasing the number of enrollees or even moving out the retirement age multiplies the existing design errors.

Similar to an IRA, the bulk of the so called "trust fund" will be composed of compounding interest (penciled in IOU's). Unlike an IRA, this interest is paid by raising taxes. It makes little overall economic difference if tax increases are in FICA or general income taxes. As the 76 million Boomers retire, combine many individuals and institutions selling various securities saved for retirement with trillions of dollars compounding interest requirements in the mis-named "Trust Fund," and the result is the prescription for an unstoppable and frightening national breakdown, literally an American social Armageddon and economic apocalypse. The future is rapidly becoming the present.

LEGISLATED REMEDIES

The presumption underlying attempts to overcome the pyramid (Ponzi) scheme is that of requiring workers to pay more into the system than they receive in benefits. These Congressional attempts fall into two general categories: increase current cash

inflows by increasing Social Security/Medicare taxes (FICA) or increase the number of young in the system. Second, to reduce cash outlays by recalculating the annual cost-of-living increases (COLA), decrease the number of eligible enrollees, and reduce the benefit levels.

Although the system currently predicts raising FICA taxes (or income taxes), raising taxes are less of a viable option because of its adverse economic implications and the likelihood of forcing more individuals into the growing underground economy. This would further reduce cash flows into Social Security while leaving the welfare burden intact. The decrease in eligible retirees is accomplished by pushing out the retirement age (more will die, and pay in more and longer—a variant of the proposed "die earlier" solution) and, increasingly, by using an income, "means," test to screen out individuals. Congress has increased the number in the system by adding workers not otherwise in the system—government, farmers, and religious employees for example—and, most notably, by increasing population growth, chiefly through mass-immigration.

The plan to remedy the funding dilemma by moving out the retirement age has been accomplished previously (i.e., removing people from the retirement program). Further aging continues to be a proposed remedy. The argument is that people are living longer. This is true, but avoids two misleading aspects. First, it is political doublespeak, for it literally means that people are not leaving the system in a timely fashion, i.e., not dying early enough—as stated in a proposal. Second, that there is a funding dilemma and the proposed remedy is to have the Boomers pay longer and more into the system, while delaying, reducing or removing the promised payments.

Because the Budget and other proposals emphasize the role of population growth in salvaging Social Security, the balance of my remarks will concentrate on population growth and briefly discuss several ramifications. I begin by briefly discussing population growth and the role immigration plays in that growth, then the worker/retiree ratio, attempts to increase cash inflows, and finally several unintended consequences of our current high immigration policies. The conclusion will be that these attempts to mitigate the ills of the program only serve to exacerbate existing problems and generate additional concerns as well.

POPULATION GROWTH

When future historians write about U.S. population growth and the subsequent decline of America, they will write that the single greatest tragedy in U.S. history was the change in immigration policy in the mid 1960's.

Without over immigration the U.S. would be on a very welcome trajectory to achieve a stable population, sustainable economy, and cohesive society. The consequences of this road to stabilization is that the U.S. would have had the opportunity to ameliorate or avoid several extremely serious looming problems, including Social Security, would be in a much stronger position to assist the disadvantaged within the U.S. and to facilitate change in other nations as well.

Although it is an American tragedy of epic proportions, the solution is not difficult. That Americans want to stop population growth and reduce immigration is abundantly clear. Repeated polls show that over 80% of Americans from all walks of life favor a reduction in immigration and our population to stabilize by 2050. And nearly 60% want the U.S. population reduced!

The explanation lies in the numbers:

• Were a net zero immigration (equal in and out migration) policy established in 1965, the U.S. population would have stabilized around the year 2025 at a probably sustainable and certainly more comfortable, 225 million (versus 272+ million of today). Our Social Security dilemmas would have been vastly easier to rectify.

• Had appropriate immigration reform been accomplished in 1970, the US population would have leveled off in the next century at around 247 million.

• If current immigration policy were revised at this time to a policy of zero net immigration, the U.S. population would still continue growing to reach about 310 million about the year 2030.

• If immigration were cut to about one-fifth today's level (mid Census projection), the U.S. population would continue to grow to approximately 400 million at 2050.

• Not seen in the mid Census projection of about 400 million is that the U.S. population juggernaut would continue growing until it eventually stabilized at a population of about 1.6 billion (Billion!).

• Under current population policies, the Census Bureau projects the U.S. population in only fifty years to exceed 500 million (and growing rapidly!).

• Doubling already high current immigration policies would indicate, not a population of 400 million nor a staggering 500 million but, I would think, a population on the order of 650–700 million or more in fifty years, rapidly growing, and unlikely

to achieve stability! Just how many hundreds of millions or billions does the Congress have in mind in order to save Social Security? Even with a cursory reading, it is clearly ludicrous to even consider such an ill-advised proposal.

- Were a zero net immigration policy implemented in the mid 1960's then 100% of our population growth above 225 million would have been derived from immigration.
- With present immigration policies and trends, immigrants coming after 1970 will account for at least ninety percent of all U.S. population growth by the year 2050.
- If we consider only the growth from descendants of 1970 residents (just before the huge immigration influx), the result is that all of our population growth after the year 2035 will be derived from immigrants.
- Currently, over sixty percent of U.S. population growth is from recent immigrants and their offspring.
- Population momentum indicates that *after* implementation of a population policy designed to achieve a stable U.S. population, it nevertheless requires over fifty more years before our population would actually achieve the no additional population growth mode, possibility doubling again in that time.

Regrettably, in not providing the above readily available census and INS information it would appear that those responsible for preparing the Social Security and demographic portions of the Budget and various proposals, although 1st rate professionals and certainly realizing the consequences of their work, failed to override politics with appropriate standards of professionalism.

The numbers are already unprecedented in U.S. immigration history, a further doubling, as proposed, is mind boggling! The most recent data indicate that over 1,300,000 immigrants entered the U.S. in 1997 and nearly that many last year. (The number could be considerably higher due to uncounted and illegal immigration, estimated at between 250,000 and 500,000 each year.)

Similarly, legislated attempts to promote increased fertility are equally counterproductive. For example, tax exemptions, the $500 per child tax credit, and tax credits for daycare also serve to compound the problems of U.S. population growth. The government pays to have babies. Significantly, it also has the regretful effect of reducing parental responsibility to provide for their own families, creates additional dependence on the government, and sends an erroneous message about a sustainable U.S. population.

The problem involving funding Social Security is that increased fertility aggravates the pyramid nature of the system while markedly increasing the dependency ratio. The effect is to actually reduce the wherewithal to fund Social Security.

The impacts of high immigration on our culture, society, economy, and environment must be addressed. Nevertheless, there are other compelling arguments against immigration as a remedy to our Social Security/Medicare predicament.

IMMIGRATION AND SOCIAL SECURITY: A DANGEROUSLY INCORRECT POLICY

In 1985 and again in the 1990's, because of overwhelming public support, it was widely expected that Congress would take the position of reducing immigration to traditional levels. Beginning in 1965, special interests and the retirement fund lobby mistakenly told Congress that our rate of domestic population growth was insufficient to maintain the solvency of the Social Security system. They were joined by an unlikely alliance—social groups, religious organizations, humanitarians and allied opportunists and economic and corporate powerhouses (and some also did with the objective of changing American society) to lobby Congress to thwart the wishes of the American citizen to pass this ill-advised legislation. Instead of reducing, Congress doubled the legal immigration quota and turned a deaf ear to dealing with the millions of illegal immigrants. Evidently, the failure was in understanding the pyramid nature of its design. The legislation to open a floodgate of immigration became an unseen and little known Congressional attempt to remedy the alleged funding dilemma drawing near by rapidly increasing numbers at the bottom of the worker pyramid. Moreover, advocates assume they are willing to pay into our Social Security system and are deluded into believing there are no serious side effects. As described earlier, it was an inappropriate policy initially; the situation worsens with each passing day.

For a moment, let's step back to put the apparent demographic and Social Security complication in perspective. It is a passing predicament. The population "Boomers" are the well known visual depiction of a large "population" lump passing through a snake. The image also illustrates the ethereal nature of the demographic concern. At each stage of their lives, these baby-boomers required the economy and

society to accommodate the necessary, but transient, changes. The point is that this passing phenomena is just that, temporary and it is exceedingly unwise to make permanent government policy based on transitory demographic situations. The repercussions of any alleged short term remedies are dreadfully frightening when considering the lasting affects of population growth.

The current budget and some proposals, like the immigration legislation of the last nearly thirty years, is a gallant legislated attempt to continue shielding the public from realizing the program may require wholesale modifications, if not total scrapping.

However, there is a more subtle agenda at work as well. It is a manifestation of the "die earlier" notion. These same immigrants have a life expectancy less than the citizens approaching retirement. Some proponents may say one thing, but they plan on a disproportionate number of these new immigrants, other minorities, and other disadvantaged, dying prior to receiving a retirement pension. Likewise, they overlook the millions of illegal aliens because, in addition to limiting wage demands, they may pay into the Social Security retirement program yet are precluded from claiming benefits. On the other hand, the Clinton administration and mass-immigration allies certainly understand this dilemma. The fact that they repeatedly grant huge numbers of illegal immigrants amnesty and health, and other benefits, suggest they realize it. On the other hand, those that survive to receive a Social Security benefit reap a windfall at the direct expense of native born Americans.

Let's now examine how immigration is a perilously flawed solution to the Social Security/Medicare funding dilemma, notably the "worker/retiree" ratio and to the matter of increasing cash flows. Following that discussion will be a brief discussion several unanticipated impacts of excessive immigration on our culture, society, economy, and environment.

WORKER TO RETIREE RATIO

The alleged problem most frequently heard is that there won't be sufficient workers to support the retirees, the worker/retiree ratio, will be inadequate. Simply put, they argue our population is aging. This is often cited as an excuse to increase immigration.

Those asserting that population growth through high immigration is a solution miss the mark in using the simple relationship of retirees to workers. The more meaningful and appropriate item to examine is the dependency ratio. This ratio is the number of young plus the number of old as a percent of the total population. Thus, the dependency ratio reflects the ability of workers, the entire labor force, to provide for total dependents, young and old. (Note, of course underlying much of this is the extent of government programs.) Recall that a proposal was for the Boomers to die earlier. From the standpoint of the dependency ratio and Social Security, the ratio is enhanced by removing the elderly from the system. Although this proposal is more of an academic than actual position, we should also be aware that subtle legislative changes in the provision of health care would serve the identical function.

What is seldom acknowledged are the more significant possibilities at the other extreme, of reducing the number of young. This is where the greatest enhancement to funding Social Security lies. With our highly pro-natalist government policies this action seemingly would be met with some resistance. However, Americans have had an environmental friendly, economically sustainable, and socially desirable fertility rate for many years. Thus, there is little, if any problem associated with native born Americans. The difficulty remains with recent immigrants and their excessive birthrates. For the most part, the problem would be quickly settled by minimizing immigration. After minimizing immigration, expanded programs for recent immigrants must be passed to arrange rapid assimilation—and that process includes family planning services.

The dependency ratio of a stable population is 39%. Immigration proponents and their Social Security allies seem to think that this ratio is something to fear. Really? In 1960 when John F. Kennedy was president, the ratio was 39% and there did not appear to be any social or economic trauma associated with that ratio. During the 1970's the ratio was about 38% and during the 1980's (due to the Boomers) the ratio was around 35%. Currently the ratio is about 33% primarily due to the relatively few (now elderly) parents and grandparents of the Boomers and the "birth dearth" immediately following the Boomer generation. This somewhat reduced dependency ratio in part explains the booming success of the current national economy. If policy were modified to limit annual immigration to our traditional 150,000 the ratio would less than 38% in 2050. This is, as stated previously, is a prudent level and no cause for alarm.

Several observations can be drawn from this data. First, the dependency ratio has varied without creating Social Security unique funding problems, around the mid to upper thirties percentiles. Second, the effect of the baby-boomers moving up the demographic ladder temporarily reduced the ratio below the average range, yet without significantly nor permanently benefiting the funding of Social Security (again see "Trust Fund"). Finally, even under a slow growth or sustainable population scenario, the ratio does not climb appreciably, remaining within the historical non-problematic range. The data clearly indicates that there is no genuine case for taking action.

To clearly demonstrate how circular and preposterous the immigration approach is, let's extend their logic further out in time. To maintain a consistent ratio, the projected 2050 population of over 500 million will require immigrating 2.5–3 million fresh immigrants each year instead of the approximately 1.3 million of today. (Canada? In this short period Canada will merely become a subdivision of the U.S.!) If one assumes the worker/retiree ratios we often hear of 4,5, or 6 to 1, the numbers become obviously irrational—5, 10, 15 million or more additional immigrants every year! Who will pay their Social Security? Who will want to?

If there is any legitimacy to the claim that immigrants will bail out the Social Security/Medicare systems, any further immigration must be postponed until just prior to the predicted collapse when those fresh cash inflows will provide funds to retirees. In the interim, in order to save and preserve Social Security, the numbers should be minimized and the immediate burden reduced by revising current immigration policies to be based on the former policy of U.S. labor needs (that is of only already educated, skilled workers, certainly no older than 45, and without regard for "family unification").

A corollary to the dependency ratio are the national economic effects of the combination of the Boomers and relatively fewer numbers at either extreme. This is as good as it gets! Our current policy of over immigration provides cheap labor for a few fast food outlets, food processing and a few other retail type firms dependent on cheap and unskilled labor, but by increasing the dependency problem, aggravates funding Social Security. (There are other compelling negatives as well.) On the other hand at no time in U.S. history have there been so many educated and skilled workers, the Boomers, over a succession of years, continuing to enter their most productive years and period of highest earnings. They are extremely productive and well-off, invest, buy SUV's, larger and second homes, damage the environment, and generally propel the economy like never before and, as a group, unlikely to repeat. However, this boom will pass and the economy and society will return to a balanced and trendline rate of economic growth.

If the increase in life expectancy (forecasted to between 83 and 87 years) is also considered, even a higher dependency ratio is not cause for alarm. Unlike the young, workforce veterans are valuable to the productive capability of the economy. Aging workers can continue to work, retire later (as Social Security already recognizes) and be productive citizens over a longer period of time. Finally, because the aging Boomers are the most educated and experienced labor group in U.S. history, it would not only increase tax receipts, but support other social concerns if government were to eliminate disincentives to their continued employment.

IMMIGRATION AND CASH INFLOWS

Let's now turn to the apparently correct, "common sense," component of their proposal, fresh cash. There are two errors in this approach. The first is that because recent immigrants have significantly reduced education and skill levels, their contributions to the system are minimized even though their systemic liabilities disproportionately increase. In addition, the unprecedented numbers compel our communities and state governments to otherwise unnecessarily raise taxes and spend vast sums to provide for them—diminishing the wherewithal of local citizen taxpayers to fund other needs.

Second, is the serious timing factor. This asks the question, "why increase immigration beginning in the 1960's, then open a floodgate, and another (proposed) doubling now, when the collapse will be forthcoming after the turn of the century, around the year 2020? Immigration of the last twenty five years has created additional funding demands on the system at precisely the wrong time. These millions of recent immigrants will be retiring and thus create increasing cash demands on the Social Security system, just when the additional cash inflow is most needed!

How bad will it be? Data show that fully fifty percent of immigrants currently in the U.S. will reach retirement age by the year 2020, in the heart of the feared crunch. Compounding the error is the income redistribution and trend toward reliance on further income redistribution using, for example, a "means" test for Social Security recipients. The means (income) test, in addition to unfairness (workers be-

lieve it's their money!), will remove additional "average" American's from the system. The changing definition of "average" also results in ever increasing numbers of Americans being reconsidered as benefit recipients. On the other hand, the average income of immigrants is considerably less than that of the average native born American, thus their funding contribution to the system is disproportionately less than their numbers would otherwise suggest. Moreover, because of the income redistribution aspects, they will have accumulated significantly greater unfunded system liabilities than the average American while contributing far less.

Taxation of the Social Security pension when a retiree earns over some small threshold amount is commonplace, but ill-advised. More subtly, taxation of non-inflation adjusted benefits is another example. The point is that by increasing the number of immigrants, income redistribution aspects, and further means testing will result in exaggerating the direct transfer of earned income from native born Americans to immigrants. Once this mechanism is recognized by the public, there is very likely to be further erosion of support.

In short, the ill-considered immigration policies of the last twenty five years, rather than assisting, have actually magnified the funding problems of the Social Security system. In other words, although on the surface it appears counter intuitive, in order to help save Social Security/Medicare, immigration must cease at this time, with the option of revisiting the issue in twenty years.

Despite the inclination of Congress to solve U.S. and world problems, this unprecedented influx of immigrants will further destabilize American society and economy and provoke ethnic and intergenerational conflicts. The promise of the Social Security system to Americans, notably the Boomers, is rapidly becoming a embellishment due to immigration. These Boomers are the only group in history to have funded the system throughout their lives. Now, as they approach retirement, they are in line to be abused in order maintain a failing Social Security system.

UNANTICIPATED CONSEQUENCES OF RECENT IMMIGRATION LEGISLATION

The magnitude of immigration raises several items overlooked in the proposals. One must wonder if the Clinton Administration and Congress are prepared to sacrifice so much of America for this oversight? The unparalleled influx of immigrants also creates turbulent social problems such as a nagging high unemployment rate (only now in the final boom economic stage, subsiding), reductions in average wage levels, widening income gaps between the lower skilled and higher skilled worker- and calls for social legislation to redress this apparent development, and that many migrants arrive with an allegiance and purpose of a foreign nation in mind are also important considerations. Furthermore, the population induced ecological damage will be massive, expensive to repair, and sometimes irreparable to the U.S. and world environments. It is policy not destiny.

Current excess immigration policies has the worrisome attribute of reducing access to or even diminishes social programs and economic opportunities for the less well-off American citizen, most gravely Blacks. Those "Great Society" programs, for example, intended to facilitate Blacks and other disadvantaged Americans transitioning into mainstream America are increasingly utilized by immigrants. It is quite disconcerting that proponents disconnect the problems associated with high immigration with its effects on American Blacks and disadvantaged. Over immigration directly disadvantages the poor in U.S. society. Wouldn't it produce a much more pleasant and well disposed society if our government policy changed from educating and encouraging immigrants to educating and building skills for disadvantaged native born Americans?

These more skilled individuals, I will add, would increasingly contribute to Social Security without many of the environmental and social repercussions. Moreover, in reaching out to the other disadvantaged native born American citizens', this action would decrease welfare costs and provide additional cash flow into Social Security, meanwhile reducing income inequality and increasing overall standards of living.

Furthermore, it is sad to note that when our immigration laws were changed in the mid 1960's, the standard for unemployment was three percent and only when the three percent level was breached did economist and the government become concerned about rising unemployment. Beginning in the 1960's, on the other hand, the unemployment standard was raised to an incredibly high five percent, for the most part, in order to accommodate the revised immigration legislation. That two percent (or more) difference represents large numbers (millions) of American poor and disadvantaged, often Black, having their futures obstructed by Congress with its ill-conceived immigration policies. I am certain that our Congress (and the current Ad-

ministration) failed to comprehend the disastrous racial overtones connected with their ill-conceived effort to rescue Social Security via high immigration.

There is another complication as well. Our mass-immigration policies since 1965 are inconsistent with traditional American immigration policies of moderation, preserving the American culture, and of balance. The dissimilarities can be seen if one compares our traditional and more recent source nations. The impact on the demographic structure of America is quite illuminating, revealing that the United States is quickly losing its European heritage.

The mis-guided efforts to salvage a self-destructive retirement system sets up a less than pleasant scenario. Can the Committee members imagine how these immigrants and their descendants will react when the system which used them as instruments to save it, now crashes upon them, in no small measure because of them? Contemplate the implications as Boomers retire, 10, 15, 20, 25 years from now and how it will be acted out by those frustrated and less well off but rapidly growing masses. Picture in your mind large numbers of relatively well off whites plus some Blacks and Asians (i.e., today's native born Americans), now absolutely and relatively declining in numbers receiving a Social Security retirement pension from an enormous and rapidly growing much less well-off largely immigrant and disadvantaged population highly envious of the elderly (Boomer) generation and very likely coming to understand a Social Security (and political) system that has seduced and coerced them into paying for the Social Security retirement pensions of the system that is destined to betray them. The ability of immigrants and their supporters to influence legislation is being felt today; in coming years, that influence will be powerfully expressed in a variety of outcomes.

This observation may help to explain why Americans of all kinds, feel it in their and the nation's best interest to return to traditional immigration policies. If the Boomers and Generation "X'rs" of today are skeptical of receiving their Social Security/Medicare contributions, consider the impossibility of future generations and that they, unlike today, will be fully aware that their promised pensions will be but delusional dreams of a well intentioned but exceedingly ill-advised Congress.

CONCLUDING COMMENTS

I want to thank you again for an opportunity to present this Testimony and hope this information will make a useful contribution to your deliberations.

My remarks began by noting that the fundamental design of the Social Security/Medicare system was profoundly flawed and provided illustrations clearly demonstrating that proposals to increase U.S. population were ill-advised and in great measure multiplied the existing predicament. I also mentioned that any increase in enrollees, especially using high immigration is a dangerously flawed notion. The current and proposed immigration policies are deleterious to the nation and to its economic, cultural and social fabric and will result in chaos in Social Security.

An approach contrary to the current one of unprecedented population growth is appropriate and necessary: minimizing new enrollees such as workers currently not enrolled and limiting further immigration while also assisting recent immigrants to rapidly assimilate is a critical first step. Protecting our environmental legacy, increasing national cohesiveness, and providing a thriving economic platform can only be accomplished with a population balanced across age groups.

Programs and current proposals undertaken by Congress to remedy Social Security have often worked in opposition to achieving these sound national goals while further destabilizing Social Security.

I will be happy to answer any questions you may have or to provide additional information.

Statement of Dr. John C. Goodman, President, National Center for Policy Analysis

The new Social Security Guarantee Plan put forward by Reps. Bill Archer and Clay Shaw has a worthy aim: to secure future retirement benefits for today's young people without increasing taxes on workers or reducing benefits to retirees.

To fully appreciate the importance of the plan, consider what will happen if we don't do anything. According to the Social Security Trustees, by the year 2045, when today's 21-year-olds will be retiring, the payroll tax needed to pay Social Security benefits will be more than 70 percent higher than it is today. Whereas the current system takes about 10 per cent of workers' incomes to pay retirement pensions, in the future the government will need about 17 cents out of every dollar. This tax

won't be imposed in a vacuum. When the cost of Medicare and other government health programs for the elderly are added in, taxes will take almost one-third of everything workers earn, just to pay benefits under current law. That's before we build any roads, or pay the salaries of police and teachers, or do anything else. Will future taxpayers, most of whom are not yet born, be willing to bear that kind of tax burden? It's unlikely.

The Social Security Guarantee Plan offers a better way. Under this plan, workers would continue to pay (with their employers) 12.4 percent in Social Security payroll taxes. However, workers would receive an income tax refund equal to 2 percent of wages, which would be invested every year in a private investment account of stocks and bonds. This would be a refundable income tax credit, so workers who don't earn enough to pay taxes would get a "refund" from the government to fund their private accounts. Workers could choose from among 50 private investment firms to manage their accounts. These firms would be required to invest conservatively in a diversified portfolio.

Upon retirement, a retiree's benefits would come from two sources: an annuity based on the private account and the Social Security system. A government guarantee would insure that everyone receives a retirement income at least equal to Social Security's promised benefit. For example, if a retiree's private investment is only enough to pay 80 per cent of his or her retirement benefit, the government will pay the other 20 per cent.

A controversial feature of the Social Security Guarantee Plan is that it requires individuals to turn their account balances over to the government at retirement. The government then pays them a monthly annuity. Letting private annuities handle the job makes more sense.

Can the Social Security Guarantee Plan accomplish its proclaimed goal of maintaining the Social Security program without cutting benefits or raising taxes? Can it at the same time eliminate the massive unfunded liability that now exists? The Social Security Administration has evaluated the plan and said yes. However, the Social Security Administration's analysis treats the IOUs in the OASI Trust Fund as real assets that can be used to pay those benefits as they come due. In fact, every asset of the Trust Fund is a liability of the Treasury. So the only way to redeem the IOUs in the Trust Fund, unless there is a surplus, is to raise taxes. This will be the problem at the time of the retirement of the baby boomers.

The National Center for Policy Analysis has analyzed the plan is a different way. Our analysis assumes that the unified budget surplus will be used as a source of funding for deposits to the Social Security Guarantee Accounts (SSGAs), the personal accounts set up under the plan. It also assumes that the new revenue made possible by the addition to the nation's capital stock by the private accounts will be sequestered as needed to pay benefits in future years. Both these assumptions are consistent with the spirit of the Social Security Guarantee Plan.

We have used a simulation model developed by economists at Texas A&M University for the National Center for Policy Analysis. Our analysis, like that of the Social Security Administration, assumes a real rate of return on the private accounts of 5.35%.

The NCPA analysis finds that the Social Security Guarantee Plan can provide the benefits promised by current law for retirees and their families (including future adjustments for inflation) while eliminating our current massive unfunded Social Security liability. Furthermore, by the time today's new workers retire, those just entering the workforce can anticipate a lower payroll tax than today, rather than the 70 percent increase in the payroll tax that can be expected if we retain the current Social Security system.

The following table shows the average percentage of new retirees' benefits that will be funded from personal account accumulations in various years under the plan.

The Contribution of Personal Account Annuities

Year	New Retirees: Percent of Monthly Benefit Funded by Private Accounts
2010	4%
2020	12%
2030	26%
2040	42%
2050	51%
2060	50%
2070	49%
2075	48%

It is fairly widely recognized that the specter of intergenerational conflict looms as a legacy of the Social Security system in its current form. Too many proposed reforms would offer solutions that harm the elderly by reducing benefits or harm the nation's workers by increasing payroll taxes, or do both. It has long been our contention that the system can be reformed without either of these drastic recourses. The Social Security Guarantee Plan is an approach that can accomplish that kind of reform.

Statement of Darcy Ann Olsen, Entitlements Policy Analyst, Cato Institute

Cato Briefing Paper No. 47, June 11, 1999, Social Security Reform Proposals: USAs, Clawbacks, and Other Add-Ons

Executive Summary

Faced with Social Security's impending deficits, some lawmakers have proposed supplementing the program's benefits with personal, market-based retirement accounts for all workers. Those proposals, dubbed "add-ons" because they would be added to the existing Social Security system, do not address Social Security's financial crisis. They would merely create another centralized retirement plan requiring a new funding stream.

Proposed funding sources include voluntary individual contributions, general tax revenue, and mandatory payroll tax increases. Depending on which funding mechanism is selected, the market-based retirement accounts threaten to become tax shelters for higher-wage earners, become new entitlements, or increase the payroll tax burden. Although some add-ons are designed to "shore up" Social Security by cutting its benefits by the amounts accumulated in the accounts, such plans rely on a vast infusion of government money and offer no greater retirement income for workers.

Studies show that if workers could invest what is currently taken from them in the form of Social Security payroll taxes, they would retire comfortably. Since workers already save enough to secure a comfortable retirement, it would be more sensible to let them get a better deal on their current payroll taxes by putting that money in personal accounts. Those accounts can be integrated with Social Security and therefore have the potential to eliminate Social Security's financial crisis. In addition, the accounts can ensure that all workers, not just the wealthy, can retire with financial security.

Introduction

In his 1999 State of the Union Address, President Clinton proposed what he termed Universal Savings Accounts (USAs) as a way to improve retirement security for workers. His proposal is one of dozens that recognize that workers should have the chance to increase their private retirement savings by owning personal, market-based retirement accounts. Although most members of Congress seem to agree that workers should own personal retirement accounts, there is some disagreement about how the accounts should be funded.

For instance, President Clinton would fund new accounts through a method called an "add-on." As its name suggests, an add-on would require workers to pay an additional amount of money, supplementary to the 12. 4 percent Social Security tax, to

establish new accounts. Proposed resources for add-on accounts include voluntary contributions by individuals, mandatory increases in the payroll tax, and general tax revenue. In the case of USAs, the funding source would be a combination of general tax revenue and voluntary individual contributions. In one plan proposed by two members of the 1994–96 Advisory Council on Social Security, the funding source would be a mandatory increase in the payroll tax. The common element of add-on proposals is that they require workers to contribute money above and beyond what they are currently forced to pay to Social Security.

The fundamental drawback with most add-ons is that they do not address Social Security's problems. Add-ons have no more to do with reforming Social Security than do Roth individual retirement accounts or any other private retirement plan; they would simply be one more personal retirement vehicle. If such accounts are established, Social Security's date of reckoning will not change by a day: the system will still face a $9.5 trillion unfunded liability requiring estimated benefit cuts of 30 percent or tax increases of more than 5 percentage points.[1] And depending on how they are financed, add-ons could increase the payroll tax burden, become a new entitlement, or become a tax shelter for higher-wage earners, while doing little to improve retirement security for workers. For example, if contributions were voluntary, evidence from 401(k) plans indicates that half of workers earning less than $35,000 would probably not participate. That would effectively create a tax shelter for higher-wage earners but would not improve retirement security for lower-wage workers. Some add-ons, like the one proposed by House Ways and Means Committee chairman Bill Archer (R–Tex.) and Social Security Subcommittee chairman Clay Shaw (R–Fla.), are designed to "shore up" Social Security by cutting benefits by the amounts accumulated in the accounts at retirement, but such plans rely on a vast infusion of government money and offer no greater income for workers at retirement.

A better way to fund personal accounts is to allow workers to use existing payroll taxes that are currently slated for Social Security. This method of financing personal accounts is known as a "carve out." The distinctive feature of carve-out accounts is that they do not require workers to contribute additional money to what they already pay into Social Security. Instead, such accounts would be funded by redirecting a portion of the current payroll tax to new retirement accounts. For that reason, those accounts avoid the add-on pitfalls: tax hikes, new entitlements, and de facto advantages for the wealthy. Furthermore, such accounts are clearly integrated with Social Security and therefore have the potential to eliminate Social Security's financial crisis. These accounts will increase the private savings of all workers, thereby reducing dependence on Social Security and explicitly reducing Social Security's liabilities. Carve-outs can ensure that all workers, not just the wealthy, have the opportunity to save and retire with financial security.

Universal Savings Accounts and Other Voluntary Accounts

The idea of establishing individual accounts funded by voluntary contributions is a favorite among politicians because they can talk about the positive aspects of individual accounts-worker empowerment, personal ownership, and wealth creation-while avoiding altogether the unpleasant but central issue of Social Security reform. In the end, these plans simply call for greater contributions from working Americans but ignore Social Security's financial crisis. If Congress established voluntary accounts, Social Security's unfunded liability would not change by a penny: the program would still face a $9.5 trillion liability because the new accounts would not bring revenue into the system or reduce benefit obligations to beneficiaries. In addition, as this section illustrates, those accounts will likely do little, if anything, to improve retirement security for the low-income workers whom they are designed to benefit.

The best-known proposal for voluntary accounts is President Clinton's Universal Savings Accounts. USAs would be funded through a combination of government deposits and voluntary individual contributions. In general, workers and nonworking spouses in low- to moderate-income households would receive an automatic government contribution of $300.[2] The automatic contribution would be phased out as incomes rose-at between $20,000 and $40,000 for singles, $30,000 and $50,000 for head of household filers, and $40,000 and $80,000 for joint filers.[3] Workers could also make voluntary contributions to their accounts that would be matched progressively by government contributions. The matching contribution would be dollar-for-dollar and would be reduced to 50 percent over the same income ranges as the automatic contribution. It would then remain at 50 percent until the income level at which eligibility ends.[4] Total contributions to an account, including government and worker contributions, are capped at $1,000 per year per person.

Participation in USAs is likely to be anything but universal. Only low- to moderate-income workers would receive the automatic $300 government deposit; however, most low- to moderate-income workers would not benefit from the voluntary component and corresponding government match, because they would not be able to afford the requisite contribution. In fact, as this section documents, experience with 401(k) plans indicates that low-income workers, who most need additional retirement income, will be the least likely or able to take advantage of the voluntary (and largest) portion of USAs.

Low incomes present the most fundamental obstacle to saving. The truth is that salaries of low-income workers barely cover basic living expenses.[5] According to the 1998 Retirement Confidence Survey, conducted by the Employee Benefit Research Institute, one in three Americans is not saving for retirement. By far the most common reason given for not saving is "too many current financial responsibilities."[6] Some 40 percent of workers said they could not save even an extra $20 per week for retirement.[7] Opening accounts for workers will not change that: workers who are either unable or unwilling to save more will not begin to do so simply because the government opens an account in their name.[8]

It is no surprise that the more one earns, the more likely one is to save for retirement. For example, only 6 percent of households with incomes of less than $10,000 have retirement accounts compared with 24 percent of households with incomes ranging from $10,000 to $24,999. Figure 1 shows the percentage of households (by income) that own retirement accounts. Similarly, the more one earns, the more likely one is to save and invest in capital markets. Figure 2 shows the percentage of households (by income) that own mutual funds and stocks.

One reason there is widespread support for policies that would encourage individual retirement savings is that so few low-income households have managed to accumulate retirement assets, which makes those households dependent on Social Security for most of their retirement income. The Social Security Administration reports that 30 percent of retirees depend on Social Security for more than 90 percent of their retirement income.[9] Will USAs, as President Clinton put it, "make real retirement security universal"?[10]

To answer that question, it is instructive to examine worker participation rates in 401(k) plans in which employers match employee contributions. Research on worker participation in 401(k) plans with employer matches is relevant to the discussion of USAs because USAs would have important features of 401(k) plans. USAs would be offered through employers, and the government would match worker contributions to varying degrees. Contributions would go into market-based retirement accounts.[11] Never-theless, 401(k) plans with matches are not a perfect analogy with USAs. For instance, several factors that influence participation rates in 401(k) plans, such as loan provisions, investment choices, and hardship withdrawal provisions, have not been examined.[12] Variation in match rates, eligibility phaseout ranges, shifts in savings, and differential tax treatment could also affect participation data. Furthermore, basing estimates of expected participation rates in USAs on participation rates in 401(k) plans with an employer match could lead to overgenerous estimates. That is because participation rates in those 401(k) plans are significantly higher than participation rates in similar savings and retirement plans such as IRAs, regular 401(k) plans, stocks, and mutual funds. On balance, however, participation in 401(k) plans is the best available model and offers a reasonable starting point for figuring out who could be expected to participate in the voluntary component of USAs and similar voluntary accounts.

Not surprising, one of the most important determinants of 401(k) participation rates is income level.[13] Figure 3 shows rates of participation by income in 401(k) plans with an employer match. Of workers offered a 401(k) plan with an employer match, 39 percent of those earning less than $15,000 annually participate, whereas 53 percent of those earning $15,000 to $25,000 participate. Contribution rates also vary with income, from a mean rate of 5 percent of salary for participants with incomes of less than $15,000 to more than 7 percent for participants with incomes of $50,000 or more.[14]

If 401(k) plans with matches give a reasonable indication of participation in USAs and similar accounts, policymakers can expect that participation rates will be significantly lower among low-and moderate-income workers than among higher-income workers. As Figure 4 shows, at least one of two workers earning $35,000 or less would not participate, either by choice or because of financial constraint.[15] An estimated three of four workers earning more than $35,000 would participate. Altogether an estimated 40 percent of workers would not participate-a number that hardly indicates universal participation.

Proponents of USAs point to experience with Individual Development Accounts (IDAs) in an attempt to demonstrate that low-income workers could save at rates

equal to those of higher-income workers, despite the fact that most do not do so currently. That assumption is based on the theory that savings rates are driven largely by institutionally structured incentives rather than by income. Most IDAs, which were a driving force behind the proposal for USAs, are matched savings accounts designed to help low-income workers build assets for such purposes as buying a first home, education, or starting a new business.[16] IDAs and USAs share several important features. Both (1) target lower-income workers, (2) encourage participation through generous matches, (3) use institutional savings mechanisms such as the government and employers to make participation easy, and (4) provide financial education information.

According to researchers at the Center for Social Development at Washington University in St. Louis, Missouri, the first major study of IDAs was the American Dream Demonstration (ADD), initiated in 1997.[17] The study involved 13 private organizations that were selected to design, implement, and administer IDAs in their communities. Unfortunately, there is little evidence to date that either demonstrates or disproves the effectiveness of IDAs. Thus far, the median value of the closing balances in the ADD is $80 (participant savings) or $224 (participant savings, interest, and matching funds). There are no significant differences in total IDA account balances by gender, residence, educational attainment, employment status, marital status, or monthly income.[18] Those findings contrast starkly with individual retirement accounts, savings accounts, and 401(k) plans. As the researchers put it, "Standard economic theory would not predict this uniformity, especially across education, employment, and income levels." They conclude, "It is far too early in the ADD evaluation to draw conclusions, but this pattern of savings and IDA balances . . . may suggest that the IDA program itself, more than individual characteristics, may be determining amounts of savings."[19] Given that the ADD evaluation is in its earliest stages, it would be premature to draw any lessons from the results.

Although the ADD study was the first major attempt to show the effectiveness of IDAs, a few small demonstration projects have also attempted to do so. For example, Brian Grossman of the Corporation for Enterprise Development writes, "Data from the National Federation of Community Development Credit Unions (NFCDCU) proves that the poor can and do save money."[20] That remains to be seen. In fact, the NFCDCU says its data are not available to the public. Such a statement prevents researchers from verifying that claim.[21] Most other IDA programs are too new to have been studied or do not plan to study participants.[22] Even if a handful of IDA programs has been successful, it would be difficult to extrapolate the results to the population at large because participants are self-selecting.[23] In sum, a much more thorough investigation of IDAs would be needed before policymakers could draw any sound conclusions about IDAs' ability to increase the savings of and build assets for low-income workers, particularly as a nationwide program of voluntary add-on accounts.

Although no model is perfect, participation in 401(k) plans with employer matches gives policymakers a reasonable estimate of likely participation in USAs and other voluntary accounts. Experience with private retirement plans shows that participation rates rise proportionately with income: the greater one's income, the greater one's likelihood of participating. That means America's lowest-income workers, who most need private retirement accounts, are the least likely to participate in or benefit from voluntary add-on accounts. The reality is that many low-income workers simply earn too little or choose not to deposit significant assets in those accounts. That will not be changed by giving them a place in which to deposit money they may not have or choose to spend on other things.

Add-Ons Established with General Tax Revenue

Because many lawmakers suspect that low-income workers will not participate in voluntary accounts, they have begun to look for other sources of funding, including general tax revenue. One such proposal was introduced by Rep. John Kasich (R–Ohio), House Budget Committee chairman. His legislation, the Personal Retirement Savings Account Act of 1998, would put 80 percent of any federal budgetary surplus into Social Security Plus accounts for all workers. Workers would have a limited number of options for investing their Social Security Plus money, and they would own their accounts. The accounts would be supplementary to the Social Security system, and they would not affect the program in any way. Kasich's press release puts it this way: "These accounts would be in addition to the existing Social Security System, which would not be affected by Kasich's legislation."[24]

Kasich's proposal and others like it are politically popular, primarily because the "spin" gives them the appearance of improving Social Security (thus, the name Social Security Plus accounts), whereas, in truth, they do not touch the Social Security

system.[25] As Kasich explains, "It is a whole new way to help Americans save for retirement while at the same time setting the stage for a solution to the long-term problems facing Social Security."[26] In other words, these accounts would supplement Social Security but would not directly affect the program in any way.

Proposals that would fund personal accounts by divvying up budget surpluses are time limited; after all, how will the government fund the accounts once the surpluses have been spent? Director of the National Economic Council Gene Sperling has said that the USAs will cost $38 billion a year once they are fully established.[27] Even if low participation rates make the accounts less costly than the administration has estimated, when the surpluses dry up, either federal deposits in the accounts will stop, or, more likely, taxpayers will continue to bear the cost of an expansive new program.[28]

It is important to note that some policymakers argue that placing the surplus in personal accounts is not an entitlement but a tax cut. For example, Clinton calls USA contributions "tax credits" and has argued that "this is the right way to provide tax relief."[29] A better analysis would argue that government contributions are not "tax cuts" but "tax favors"-preferential tax treatment of workers who are willing to apply the credits to the government's retirement plan. As Deputy Secretary of the Treasury Larry Summers puts it, "This is a tax cut which individuals have no alternative but to save."[30] The refunds become a transfer or entitlement when taxpayers receive more from the government than they have paid in taxes.

Mandatory Add-Ons

Given the limits of voluntary contributions and accounts funded with general tax revenue, some policymakers hope to establish mandatory accounts that would be funded with an increase in the payroll tax. Edward M. Gramlich and Marc M. Twinney, members of the 1994–96 Advisory Council on Social Security, proposed the best-known plan of this kind.[31] Gramlich and Twinney would establish individual accounts by mandating an increase in the payroll tax of 1.6 percent.[32] Like most proponents of individual accounts, Gramlich and Twinney recognize that "somehow or other there must be some new saving soon to finance the nation's retirement system into the 21st century."[33] However, their mandatory add-on approach is a poor way to achieve that goal.

To be sure, mandating savings avoids some of the problems associated with voluntary add-ons; namely, that mandatory is not voluntary-all workers would participate. But funding individual accounts by raising the payroll tax introduces problems of its own. In particular, the payroll tax is extremely regressive, which means that it takes a larger portion of total income from low-and average-wage workers than from high-wage workers.[34] That disproportionate burden is compounded by the fact that the amount of income subject to the payroll tax is capped at $72,600.[35] Therefore, any increase in the payroll tax necessarily weighs most heavily on low-and average-wage earners, who can least afford to pay more.

Increasing the payroll tax would also reduce take-home pay, a situation that would leave workers with less money to pay for other important items such as education, home mortgages, health care, and so on. Again, low- and middle-wage workers can least afford such reductions in pay. In addition, some could actually fall below the poverty line, particularly since payroll taxes have no personal exemptions or standard deductions.

It is important to note that, unlike most add-on plans, Gramlich and Twinney's individual accounts were proposed in conjunction with other Social Security reforms, including increasing the retirement age, cutting spousal benefits, and lengthening the benefit computation period. They designed their proposal so that the revenue generated by the individual accounts would offset the benefit cuts. Gramlich and Twinney explain, "These [accounts] in effect make up for the benefit cuts and provide, on average, the same benefits as under present law."[36] Regardless of whether the combined reforms could bring Social Security into long-term actuarial balance, the Gramlich-Twinney plan does nothing to improve a host of other problems associated with Social Security and actually makes some of them worse.

For example, increasing the payroll tax without increasing benefits effectively reduces Social Security's rate of return. Already, workers born after 1970 will receive less than 1 percent return on their payroll taxes, assuming Social Security manages to pay all benefits promised under current law.[37] Laurence Kotlikoff, professor of economics at Boston University and Social Security expert, reports, "Today's 18-year-olds in every economic class will pay more in taxes than they receive in benefits."[38] If payroll taxes are increased, that rate of return will worsen further.[39]

In addition, the proposal would not alleviate the high poverty rates under Social Security. Currently, an estimated 20 percent of widowed women, divorced women,

and never-married women live in poverty while collecting Social Security. Poverty rates during retirement for African-American and Hispanic-American women are 28 percent.[40] Increasing the payroll tax will simply extract more money from those women during their working years and give them no more financial security at retirement. That is an outrageous proposition, considering that virtually all women (and men) would be better off under a system of personal retirement accounts funded through the payroll tax.[41]

Add-Ons with Clawbacks

The most recent proposals for add-on accounts include "clawbacks"-provisions that would reduce promised Social Security benefits by the amount of revenue generated by the new accounts. Like other add-ons, these accounts would require a new revenue stream.

House Ways and Means Committee chairman Bill Archer (R–Tex.) and Social Security Subcommittee chairman Clay Shaw (R–Fla.) recently proposed this approach. Under the Archer-Shaw plan, the accounts would be funded with general revenue. The government would place an amount equal to 2 percent of a worker's earnings, in the form of an income tax credit, in a personal account. For instance, a worker making $50,000 would receive a credit worth $1,000. Any revenue generated by the accounts would be offset at retirement by cutting an equivalent amount of Social Security benefits.[42] Because the amount of money that can be placed in the accounts is capped at $1,452 per year and because the plan requires 40 percent of the funds to be placed in bonds, even the highest-wage workers would be extremely unlikely to generate assets in excess of Social Security's promised benefits.[43]

Consider a person who works 40 years, contributes the maximum allowable amount per year ($1,452), and earns a 6 percent real rate of return. His account would generate an annuity worth roughly $865 per month, whereas Social Security promises to deliver roughly $1,800 per month.[44] Because the amount generated in the account is less than Social Security's promised benefits, that worker's retirement benefits would not increase. In short, the Archer-Shaw plan would require a vast infusion of general tax revenue just to make good on Social Security's promises; the additional revenue would not buy greater benefits for workers.

Regardless of whether infusing Social Security with general tax revenue could put the program into long-term actuarial balance, the clawback approach has a host of other problems. Like the Gramlich-Twinney plan, the proposal would do nothing to alleviate the high poverty rates low-wage workers face under Social Security. And, by requiring workers to pay more money into the system without increasing benefits, the proposal reduces Social Security's rate of return. Furthermore, workers would not own their accounts. If a worker dies before age 65, he can leave his account to his heirs. However, workers who retire are forced to surrender their accounts to the government in exchange for an annuity. Thus, in order to have a property right in your account, you have to die before age 65. A vast majority of workers who live to retirement would have no rights to their accounts.

Finally, workers are already paying more than enough to retire comfortably. For example, if a worker making $20,000 were able to put his payroll taxes in an account that provided an annual real return of 6 percent, he would retire with an account worth more than $380,000 after 40 years of work. Using a conservative annuity estimate, such an account would be able to provide a monthly payment of more than $1,450.[45] Social Security promises to provide such a worker with a monthly benefit of roughly $810.[46] In that light, it seems senseless to use more taxpayer funds to begin a new retirement program.

Conclusion

The idea of establishing individual retirement accounts alongside Social Security is a favorite among politicians because they can talk about the positive aspects of individual accounts-worker empowerment, personal ownership, and wealth creation-while avoiding the more unpleasant but central issue of Social Security reform. Whether funded through voluntary contributions, general revenue, or payroll tax increases, in the end those plans simply take more money from working Americans while ignoring Social Security's financial crisis. Social Security would still face a $9.5 trillion unfunded liability. Making Social Security solvent would still require estimated benefit cuts of 30 percent or tax increases of more than 5 percentage points.

Proponents of add-on accounts fail to recognize that workers are contributing enough to provide for a comfortable retirement. Dozens of studies have shown that if workers were able to invest their Social Security payroll taxes, they would retire with substantial sums in their accounts. It is senseless to force workers to pay above

and beyond what is already enough to secure a comfortable retirement. Congress should simply let workers get a better deal on their current payroll taxes by allowing them to redirect that money into personal accounts.

Notes

1. 1999 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds (Washington: Government Printing Office, 1999), p. 28.
2. The contribution would be in the form of a tax credit deposited directly into each worker's account. The credit would be "refundable," meaning a worker's credit could exceed his tax liability.
3. "President Clinton Introduces Universal Savings Accounts: Summary Documents," National Economic Council, April 14, 1999, p. 8.
4. Eligibility ends at $50,000 for single filers with pension coverage, $75,000 for head of household filers with pension coverage, and $100,000 for joint filers with pension coverage. There is no eligibility limit for people without pension coverage.
5. Sondra Beverly, "How Can the Poor Save? Theory and Evidence on Saving in Low-Income Households," Center for Social Development, Washington University, St. Louis, Missouri, Working Paper no. 97–3, 1997, p. 21, http://gw bweb.wustl.edu/users/csd/workingpapers/wp97–3.html. Beverly examines demographic variables as they relate to savings and discusses several theories of saving, including neoclassical economic, psychological, sociological, behavioral, and institutional theories.
6. Sixty-six percent of respondents said they had "too many current financial responsibilities." The second and third most common reasons were "I expect to have a pension" (26 percent) and "economic events, such as inflation and unemployment, are too uncertain" (26 percent). Paul Yakoboski, Pamela Ostuw, and Jennifer Hicks, "1998 Retirement Confidence Survey," Employee Benefits Research Institute, American Survey Education Council, and Matthew Greenwald and Associates, Washington, 1998, http://207.152. 182.56/rcs/rcs-expectations.pdf.
7. Survey participants were asked, "Could you save $20 per week more for retirement?" Forty percent of workers who had saved for retirement said no, and 41 percent of workers who had not saved for retirement said no. Paul Yakoboski, Pamela Ostuw, and Jennifer Hicks, "What Is Your Savings Personality? The 1998 Retirement Confidence Survey," Employee Benefits Research Institute Issue Brief no. 200, August 1998, p. 11, http://www.ebri.org/rcs/T114.pdf.
8. Some policymakers might argue that the tax benefits of new retirement accounts would induce workers to save; however, most low-in-come workers pay little or no income tax, so the new accounts would be unlikely to alter their propensity to save.
9. Sixty-six percent of retirees depend on Social Security for at least half of their retirement income. Social Security Administration, "Fast Facts and Figures about Social Security," p. 7.
10. "Remarks of the President on Universal Savings Accounts," White House, Office of the Press Secretary, April 14, 1999.
11. A typical employer match is 50 cents for each $1 contributed by the worker, with the match ending when worker contributions reach 6 percent of salary. William Bassett, Michael Fleming, and Anthony Rodrigues, "How Workers Use 401(k) Plans: The Participation, Contribution, and Withdrawal Decisions," National Tax Journal 11, no. 2 (June 1998): 265.
12. Ibid., p. 284.
13. Ibid., pp. 270, 276. Low-income workers have greater difficulty participating in 401(k) plans because of their low incomes. In addition, the authors cite other reasons for lower participation among low-income workers: low-income workers benefit less from the tax-deferred nature of 401(k) plans than do high-income workers; they are more likely to be liquidity constrained and therefore have better uses for their funds than retirement saving; some are more likely to be covered by means-tested programs and therefore face high implicit tax rates on savings; and Social Security income replacement rates are higher for low-income workers, reducing their incentive to save. Plan and household characteristics are also important influences on the decision to participate in 401(k) plans.
14. Ibid., p. 275.
15. The median income of households in 1996 was $35,492. Bureau of the Census, Statistical Abstract of the United States: 1998 (Washington: Government Printing Office, 1998), p. 471.
16. Virtually all the Individual Development Account proposals have been guided by work of the Corporation for Enterprise Development in Washington and the Center for Social Development at Washington University in St. Louis. See Michael Sherraden et al., "Downpayments on the American Dream Policy Demonstration: A Nation-al Demonstration of Individual Development Accounts," Center for Social Development, Washington University, St. Louis, Missouri, January 1999, pp. 3–4.
17. Ibid., pp. 1, 6.
18. Ibid., pp. 59–63.
19. Ibid., p. 66.
20. Brian Grossman, "What We Know about the Success of Individual Development Accounts," Corporation for Economic Development, Washington, March 1997, p. 5, http://www.cfed. org/idas/documents/whatweknow.htm.
21. NFCDCU would not release its data to the Cato Institute for examination after repeated requests.
22. Karen Edwards, "Individual Development Accounts: Creative Savings for Families and Communities," Center for Social Development, Washington University, St. Louis, Missouri, Policy Report, 1997, pp. 1–30.
23. Author's telephone conversation with Michael Sherraden, professor of social development at Washington University, St. Louis, Missouri, March 23, 1999.

24. John Kasich, "Kasich Introduces Bill Return-ing Surpluses to Americans for Retirement Savings," Press release, March 12, 1998.

25. See, for instance, Sen. Bill Roth (R–Del.), "Personal Retirement Accounts Act of 1998," http://thomas.loc.gov/cgi-bin/query/z?c105 :S2369. Roth would use a portion of the budget surplus to establish individual accounts based on a progressive formula.

26. Kasich.

27. Gene Sperling and Larry Summers, White House, Office of the Press Secretary, Press briefing, April 14, 1999.

28. For further discussion, see David John, senior policy analyst for Social Security at the Heritage Foundation, "Testimony before the House Committee on Commerce, Subcommittee on Finance and Hazardous Materials," February 25, 1999, http://com-notes.house.gov/cchear/hearings106.nsf/fhmmain.

29. "Remarks of the President on Universal Savings Accounts."

30. Sperling and Summers.

31. Robert M. Ball et al., "Option II: Publicly-held Individual Accounts," in Report of the 1994–1996 Advisory Council on Social Security, vol. 1, Findings and Recommendations (Washington: Government Printing Office, 1997), pp. 28–29.

32. "Defined contribution individual accounts in the amount of 1.6 percent of covered payroll would be created and funded by employee contributions. Individuals would have constrained choices on how the funds were to be invested." Ibid., p. 28.

33. Edward Gramlich and Marc Twinney, "The Individual Accounts Plan," in Report of the 1994–1996 Advisory Council on Social Security, p. 155.

34. For a discussion of how payroll taxes affect low-wage earners, see Michael Kremer, "Restructuring Social Security Taxes," Brookings Institution Policy Brief no. 40, Washington, December 1998, pp. 1–8.

35. The maximum taxable income in 1999 is $72,600. 1999 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, p. 2.

36. Gramlich and Twinney, p. 155.

37. Laurence Kotlikoff, "Privatizing Social Security," National Center for Policy Analysis Report no. 217, July 1998, p. 15.

38. Ibid., p. 12.

39. Some critics argue that the proposed increase in the payroll tax is not a "tax," because the money would be put into accounts owned by the workers. Outside the Beltway, however, most workers would consider this a tax. It reduces take-home pay, and politicians tell workers when and how to spend their money. For a detailed discussion, see Peter Ferrara and Michael Tanner, A New Deal for Social Security (Washington, Cato Institute, 1998), pp. 122–25.

40. National Economic Council Interagency Working Group on Social Security, "Women and Retirement Security," October 27, 1998, p. 12–13.

41. Darcy Olsen, "Greater Financial Security for Women with Personal Retirement Accounts," Cato Institute Briefing Paper no. 38, July 20, 1998.

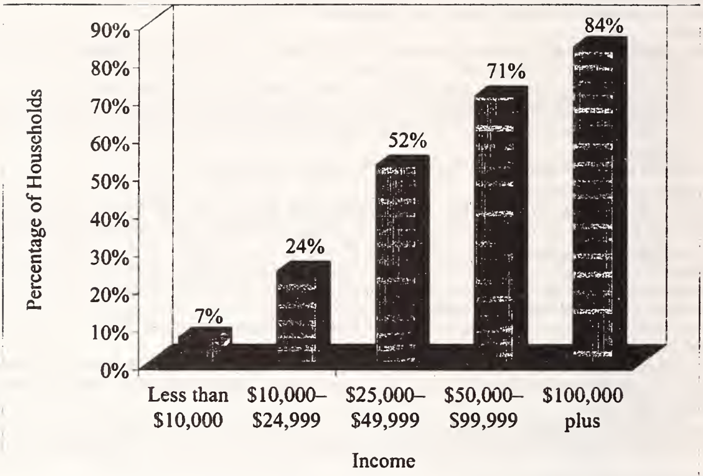
42. The credit would be "refundable," meaning that a worker's credit could exceed his tax liability. "Archer Statement on Introduction of Social Security Guarantee Plan," Committee on Ways and Means, Press release, April 28, 1999.

43. The credit is capped at the Social Security wage base, so no one would receive a credit in excess of $1,452 in 1999 (2 percent of $72,600). "The Social Security Guarantee Plan: Saving and Strengthening Social Security without Raising Taxes or Cutting Benefits," Committee on Ways and Means, Press release, April 28, 1999.

44. The annuity was calculated by using the 17.3-year life expectancy provided for a 65-year-old man in the year 2035, given on page 62 of the 1999 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds. Calculations also assume an annuitization charge of 20 percent.

45. "The Social Security Guarantee Plan."

46. Calculations by Carrie Lips, Social Security analyst, Cato Institute.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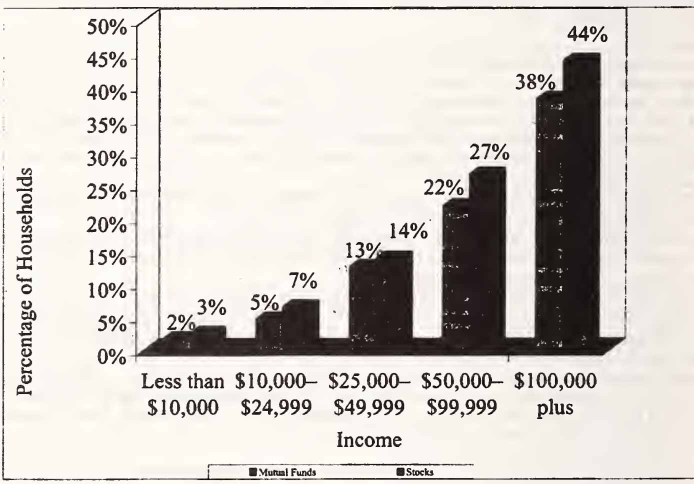
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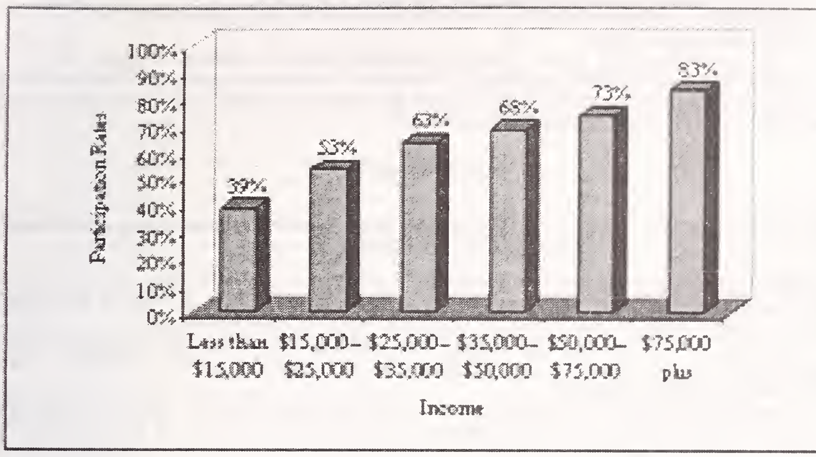

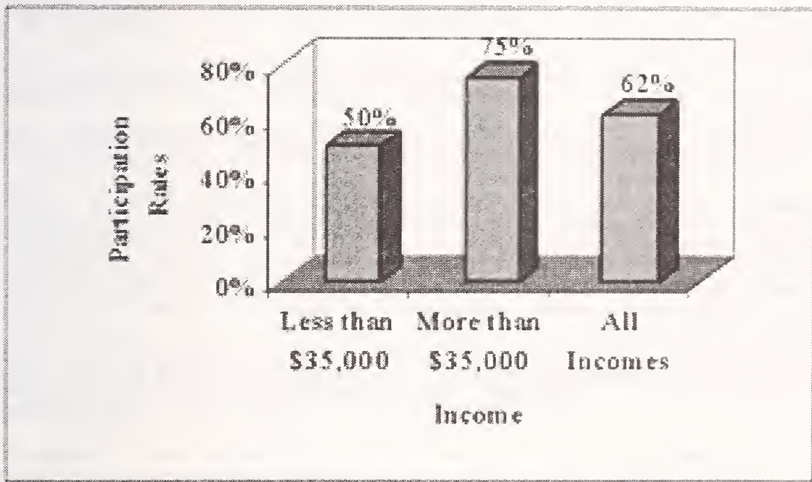

Statement of Cynthia Wilson, President, Retired Public Employees Association, Inc.

As President of the Retired Public Employees Association, an organization of more than 80,800 New York government retirees and their spouses, I am writing to commend the Committee for seeking a consensus on Social Security Reform. Our Association wishes to go on record in favor of the establishment, without delay, of a formal process for evaluating the specific proposals which will protect the retirement income of minorities, women and low-wage workers. The implementation of any such proposals should be strictly on an as-needed basis.

Specifically RPEA urges:

• The study of the "effects of increases in life expectancy on the expected level of retirement income" as proposed in Senate Bill S.21;

• The establishment of a process to implement previously evaluated reform proposals only as developing economic conditions warrant. This would include:-

—identifying those reforms having the fewest adverse effects on vulnerable populations;

—projecting the amount of income or savings generated by these reforms and;
—specifying the indicators which would justify their implementation.

RPEA also urges that:

- The Social Security Trust Funds be removed from the Federal Budget and
- Any plan establishing individual investment accounts remain outside the Social Security system, using only those budget surpluses over and above the amount attributed to the Social Security Trust Funds.

Statement of Hon. Dorcas R. Hardy, United Seniors Association; and former Commissioner, Social Security

Social Security is in serious financial trouble. By no later than 2014—just 15 years from now—the program will begin to pay out more than it collects in tax revenue. At that point, Social Security's financial crisis really begins.

By 2034, the Social Security Trust Fund will be exhausted. This insolvency date assumes, however, that the Trust Fund will be repaid the trillions of dollars owed it, which is very problematic.

According to the 1999 Trustees Report, to keep Social Security solvent for the next 75 years will require raising the payroll tax from the current 12.4% to over 18% (a 50% increase), reducing benefits by at least one-third, or some combination of the two.

These drastic measures to keep the system afloat are necessary because the worker/beneficiary ratio has changed dramatically. It was 17–to–1 in 1950, but will be only 2–to–1 in 2030.

The solution to Social Security's looming fiscal crisis is not to raise taxes. The Social Security payroll tax has exploded from 2% in 1937 to 12.4% today—a sixfold increase.

In addition, the wage base the tax rate is applied to has exploded from $3,000 in 1937 to $72,600 in 1999. As a result, today over 70% of workers pay more in payroll taxes than they do in income taxes.

Reducing Social Security benefits is also not the solution for rescuing the ailing program. With the average Social Security benefit just $780 per month, reducing benefits would cause major hardship for millions of seniors. Besides the economic impact of cutting benefits, it's wrong for the government to break its promises to seniors. Today's seniors paid into Social Security their whole lives with the expectation that they would receive a certain level of support. To change the rules now would be unfair.

Other indirect ways of cutting benefits, such as means testing, reducing cost-of-living adjustments, and increased taxation of benefits, are wrong and won't make a significant dent in dealing with Social Security's long-term liabilities, now estimated to be about $9 trillion. What they will do is hurt current beneficiaries and make Social Security an even worse deal for their children and grandchildren.

With the current system clearly unsustainable, the time has come to redesign Social Security and begin the transition to a new funded pension system based on personal retirement accounts (PRAs). Workers should be allowed the freedom to take a portion of their payroll taxes and privately invest them in stocks, bonds, and other income-producing instruments.

If forced to remain in the current Social Security system, the children and grandchildren of today's retirees face dim prospects for their own retirement years. For most young workers entering the workforce today, the real rate of return paid by Social Security will be 1% or less.

A new Social Security that incorporates PRAs will provide far more retirement income and security than the current Social Security system. Real (inflation-adjusted) returns on Social Security taxes for today's retirees are a mere 2%. Real returns on stocks since 1926 have been 7%.

To see the dramatic difference private investments can make, consider the following example given by Peter Ferrara, co-author of *A New Deal for Social Security*. If a husband and wife entering the workforce in 1985, with both earning the average income for their gender, invest most of their payroll taxes in a PRA, at a 6% real rate of return, which is less than the historical average, the couple would retire with $1.6 million in today's dollars.

Investment income alone would pay them 3 times what Social Security promises to pay, allowing them to leave the entire $1.6 million to their children. If the couple used the $1.6 million to buy an annuity, they would receive about 7 times what Social Security promises but cannot pay.

A number of bills have already been introduced in Congress by both Democrats and Republicans to redesign Social Security and establish PRAs. Five of the 13 members of the Clinton Administration's own Social Security Advisory Council (1994–96) had a plan which included PRAs.

President Clinton has proposed a plan for redesigning Social Security. While the President should be commended for putting Social Security on his agenda and for acknowledging the value of privately investing program funds to improve returns, his proposal falls far short of the mark.

One of the major concerns with the Clinton plan is the call for the government, not individuals, to do the investing. Many folks, including Federal Reserve Board Chairman Alan Greenspan, have correctly pointed out the dangers of letting the government invest workers' money in the stock market.

United Seniors Association (USA) has long advocated that, if Social Security is to survive and give workers true retirement security, the system must be redesigned. The longer Congress and the President wait, the more difficult the changes will be, especially with 77 million Baby Boomers who will soon begin collecting benefits.

With our economy strong and surpluses projected as "far as the eye can see," there is no reason not to begin reforming Social Security now.

In the battle over redesigning Social Security, USA believes that, first and foremost, the federal government must guarantee *all* benefits promised to current beneficiaries and those nearing retirement. As was noted earlier, changing the rules now would not only be unfair, but would cause unnecessary worry among seniors. We do not need a Social Security version of the unconscionable "Mediscare" campaign that we witnessed several years ago.

When establishing PRAs, USA strongly supports allowing workers to divert at least 5 percentage points of their payroll taxes to their accounts. Lesser amounts, while welcome as a starting point, are simply not sufficient and will not generate the retirement income that workers deserve and will need.

USA also believes that saving the existing Social Security program, or paying for the transition to an improved retirement system, can and must be accomplished without raising taxes, which are already too high. If revenue is needed to help finance the transition, Congress should use most of the budget surplus, now estimated to be $2.3 trillion over the next ten years.

Lastly, while some have plans which recognize that Social Security funds must be invested in the private markets, they want the federal government to do the investing. USA believes this would be a serious mistake. The federal government should not, under any circumstances, be allowed to invest workers' retirement funds, nor should the government be permitted to regulate how workers privately invest their own funds beyond that required to ensure safety and soundness.

USA commends the efforts of all those members of Congress who have put forth plans to save and improve Social Security by creating PRAs. USA urges that Congress and the President enact Social Security reform legislation into law this year. We look forward to working with you on this critical issue.

Thank you.

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